

Woodward, Inc.
Form 10-Q
July 24, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2012

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number 0-8408

WOODWARD, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

36-1984010
(I.R.S. Employer
Identification No.)

1000 East Drake Road, Fort Collins, Colorado
(Address of principal executive offices)

80525
(Zip Code)

Registrant's telephone number, including area code:
(970) 482-5811

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

As of July 19, 2012, 68,728,097 shares of the common stock with a par value of \$0.001455 per share were outstanding.

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****WOODWARD, INC.****CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS***(In thousands, except per share amounts)**(Unaudited)*

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|---------------------------------------------------------------|---------------------------------|------------------|--------------------------------|------------------|
| | 2012 | 2011 | 2012 | 2011 |
| Net sales | \$ 460,241 | \$ 438,467 | \$ 1,336,930 | \$ 1,222,408 |
| Costs and expenses: | | | | |
| Cost of goods sold | 329,451 | 304,441 | 936,354 | 858,138 |
| Selling, general and administrative expenses | 39,627 | 38,470 | 118,984 | 109,581 |
| Research and development costs | 38,958 | 29,273 | 107,197 | 80,061 |
| Amortization of intangible assets | 8,139 | 8,935 | 24,691 | 26,020 |
| Interest expense | 6,611 | 6,361 | 19,471 | 19,161 |
| Interest income | (265) | (117) | (475) | (325) |
| Other (income) expense, net (Note 15) | 12 | 249 | (1,214) | 955 |
| Total costs and expenses | 422,533 | 387,612 | 1,205,008 | 1,093,591 |
| Earnings before income taxes | 37,708 | 50,855 | 131,922 | 128,817 |
| Income tax expense | 9,406 | 14,799 | 36,452 | 38,272 |
| Net earnings | \$ 28,302 | \$ 36,056 | \$ 95,470 | \$ 90,545 |
| Earnings per share (Note 3): | | | | |
| Basic earnings per share | \$ 0.41 | \$ 0.52 | \$ 1.38 | \$ 1.32 |
| Diluted earnings per share | \$ 0.40 | \$ 0.51 | \$ 1.36 | \$ 1.29 |
| Weighted Average Common Shares Outstanding (Note 3): | | | | |
| Basic | 68,922 | 68,793 | 68,973 | 68,785 |
| Diluted | 70,319 | 70,166 | 70,446 | 70,155 |
| Cash dividends per share paid to Woodward common stockholders | \$ 0.08 | \$ 0.07 | \$ 0.23 | \$ 0.20 |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**WOODWARD, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS***(In thousands)**(Unaudited)*

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-----------------------------------------------------------------------------|-----------------------------------------|-------------|----------------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Net earnings | \$ 28,302 | \$ 36,056 | \$ 95,470 | \$ 90,545 |
| Other comprehensive earnings: | | | | |
| Foreign currency translation adjustments | (13,565) | 8,414 | (14,018) | 17,043 |
| Taxes on changes on foreign currency translation adjustments | (1,166) | (875) | 2,127 | (1,791) |
| | (14,731) | 7,539 | (11,891) | 15,252 |
| Reclassification of realized losses on derivatives to earnings | 43 | 57 | 131 | 172 |
| Taxes on changes on derivative transactions | (16) | (22) | (50) | (65) |
| | 27 | 35 | 81 | 107 |
| Minimum retirement benefit liability foreign currency exchange rate changes | 9 | (90) | 91 | (268) |
| Total comprehensive earnings | \$ 13,607 | \$ 43,540 | \$ 83,751 | \$ 105,636 |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**WOODWARD, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS***(In thousands, except per share amounts)**(Unaudited)*

| | June 30, 2012 | September 30, 2011 |
|-----------------------------------------------------------------------------------------------|--------------------------|-------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 39,903 | \$ 74,539 |
| Accounts receivable, less allowance for losses of \$4,891 and \$2,322, respectively | 300,661 | 297,614 |
| Inventories | 423,994 | 381,555 |
| Income taxes receivable | 8,300 | 2,456 |
| Deferred income tax assets | 38,692 | 38,270 |
| Other current assets | 40,689 | 23,359 |
| Total current assets | 852,239 | 817,793 |
| Property, plant and equipment, net | 214,146 | 206,725 |
| Goodwill | 460,509 | 462,282 |
| Intangible assets, net | 243,493 | 268,897 |
| Deferred income tax assets | 8,100 | 10,466 |
| Other assets | 15,750 | 15,271 |
| Total assets | \$ 1,794,237 | \$ 1,781,434 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Short-term borrowings | \$ 5,000 | \$ |
| Current portion of long-term debt | 7,549 | 18,374 |
| Accounts payable | 120,893 | 123,453 |
| Income taxes payable | 3,394 | 5,440 |
| Deferred income tax liabilities | 800 | 74 |
| Accrued liabilities | 98,556 | 133,516 |
| Total current liabilities | 236,192 | 280,857 |
| Long-term debt, less current portion | 401,250 | 406,875 |
| Deferred income tax liabilities | 85,547 | 85,911 |
| Other liabilities | 90,589 | 88,694 |
| Total liabilities | 813,578 | 862,337 |
| Commitments and contingencies (Note 19) | | |
| Stockholders' equity: | | |
| Preferred stock, par value \$0.003 per share, 10,000 shares authorized, no shares issued | | |
| Common stock, par value \$0.001455 per share, 150,000 shares authorized, 72,960 shares issued | 106 | 106 |
| Additional paid-in capital | 95,913 | 81,453 |
| Accumulated other comprehensive (loss) earnings | (8,093) | 3,626 |
| Deferred compensation | 4,323 | 4,581 |
| Retained earnings | 1,029,188 | 949,573 |
| | 1,121,437 | 1,039,339 |

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| | | |
|-------------------------------------------------------------------------------------------------|--------------|--------------|
| Treasury stock at cost, 4,232 shares and 4,070 shares, respectively | (136,455) | (115,661) |
| Treasury stock held for deferred compensation, at cost, 275 shares and 315 shares, respectively | (4,323) | (4,581) |
| Total stockholders equity | 980,659 | 919,097 |
| Total liabilities and stockholders equity | \$ 1,794,237 | \$ 1,781,434 |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**WOODWARD, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS***(In thousands)**(Unaudited)*

| | Nine-Months Ending June 30, | |
|----------------------------------------------------------------------------------------|----------------------------------------|-------------|
| | 2012 | 2011 |
| Cash flows from operating activities: | | |
| Net earnings | \$ 95,470 | \$ 90,545 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization | 53,870 | 57,299 |
| Net (gain) loss on sales of assets | (84) | 429 |
| Stock-based compensation | 6,680 | 5,370 |
| Excess tax benefits from stock-based compensation | (3,778) | (2,581) |
| Deferred income taxes | 91 | (1,011) |
| Loss on derivatives reclassified from accumulated comprehensive earnings into earnings | 131 | 172 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (8,003) | (11,922) |
| Inventories | (46,918) | (77,389) |
| Accounts payable and accrued liabilities | (19,284) | (16,126) |
| Current income taxes | (4,168) | 10,434 |
| Retirement benefit obligations | (766) | (3,230) |
| Other | (9,588) | (5,190) |
| Net cash provided by operating activities | 63,653 | 46,800 |
| Cash flows from investing activities: | | |
| Payments for purchase of property, plant, and equipment | (44,224) | (32,640) |
| Proceeds from sale of assets | 231 | 30 |
| Business acquisitions, net of cash and marketable securities acquired | | (38,698) |
| Business acquisitions, marketable securities acquired | | (8,463) |
| Proceeds from the sale of marketable securities | | 8,217 |
| Net cash used in investing activities | (43,993) | (71,554) |
| Cash flows from financing activities: | | |
| Cash dividends paid | (15,855) | (13,764) |
| Proceeds from sales of treasury stock | 5,754 | 2,078 |
| Payments for repurchases of common stock | (31,881) | (6,837) |
| Excess tax benefits from stock compensation | 3,778 | 2,581 |
| Borrowings on revolving lines of credit and short-term borrowings | 185,129 | 126,098 |
| Payments on revolving lines of credit and short-term borrowings | (180,189) | (103,158) |
| Payments of long-term debt | (16,440) | (16,500) |
| Payment of debt financing costs | (2,185) | |
| Net cash used in financing activities | (51,889) | (9,502) |
| Effect of exchange rate changes on cash and cash equivalents | (2,407) | 1,275 |
| Net change in cash and cash equivalents | (34,636) | (32,981) |

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| | | |
|--------------------------------------------------|-----------|-----------|
| Cash and cash equivalents at beginning of period | 74,539 | 105,579 |
| Cash and cash equivalents at end of period | \$ 39,903 | \$ 72,598 |

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(In thousands)

(Unaudited)

| | Number of shares | | | | | Accumulated other comprehensive (loss) earnings | | | | | Stockholders equity | | | | |
|----------------------------------------------------------------|------------------|--------------|----------------|-----------------------|--------------|-------------------------------------------------|------------------------------------------|---------------------------|---------------------------------------------------|------------------------------------------------|-----------------------|-------------------|------------------------|-----------------------------------------------|---------------------------|
| | Preferred stock | Common stock | Treasury stock | deferred compensation | Common stock | Additional paid-in capital | Foreign currency translation adjustments | Unrealized gains (losses) | Minimum retirement benefits liability adjustments | Total accumulated other comprehensive earnings | Deferred compensation | Retained earnings | Treasury stock at cost | Treasury stock held for deferred compensation | Total stockholders equity |
| Balances as of October 1, 2010 | | 72,960 | (4,223) | (356) | \$ 106 | \$ 73,915 | \$ 23,152 | \$ (627) | \$ (16,183) | \$ 6,342 | \$ 4,888 | \$ 835,919 | \$ (113,088) | \$ (4,888) | \$ 803,194 |
| Net earnings | | | | | | | | | | | 90,545 | | | | 90,545 |
| Cash dividends paid | | | | | | | | | | | (13,764) | | | | (13,764) |
| Purchases of treasury stock | | | (242) | | | | | | | | | | (7,961) | | (7,961) |
| Sales of treasury stock | | | 310 | | | (1,754) | | | | | | | 4,963 | | 3,209 |
| Tax benefit attributable to exercise of stock options | | | | | | 2,581 | | | | | | | | | 2,581 |
| Stock-based compensation | | | | | | 5,370 | | | | | | | | | 5,370 |
| Purchases of stock by deferred compensation plan | | | 2 | (2) | | 33 | | | | | 128 | | | (128) | 33 |
| Distribution of stock from deferred compensation plan | | | | | | | | | | | | | | 445 | |
| Foreign currency translation adjustments | | | | | | | 17,043 | | | 17,043 | | | | | 17,043 |
| Reclassification of unrecognized derivative losses to earnings | | | | | | | | | | | | | | | 172 |
| Minimum retirement benefits liability adjustments | | | | | | | | | (413) | (413) | | | | | (413) |
| Taxes on changes in accumulated | | | | | | | (1,791) | (65) | 145 | (1,711) | | | | | (1,711) |

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| | | | | | | | | | | | | | | | |
|----------------------------------------------------------------|--------|---------|-------|--------|-----------|-----------|----------|-------------|------------|----------|--------------|--------------|------------|------------|--|
| other comprehensive earnings | | | | | | | | | | | | | | | |
| Balances as of June 30, 2011 | 72,960 | (4,153) | (315) | \$ 106 | \$ 80,145 | \$ 38,404 | \$ (520) | \$ (16,451) | \$ 21,433 | \$ 4,571 | \$ 912,700 | \$ (116,086) | \$ (4,571) | \$ 898,298 | |
| Balances as of October 1, 2011 | 72,960 | (4,070) | (315) | \$ 106 | \$ 81,453 | \$ 22,103 | \$ (484) | \$ (17,993) | \$ 3,626 | \$ 4,581 | \$ 949,573 | \$ (115,661) | \$ (4,581) | \$ 919,097 | |
| Net earnings | | | | | | | | | | | 95,470 | | | 95,470 | |
| Cash dividends paid | | | | | | | | | | | (15,855) | | | (15,855) | |
| Purchases of treasury stock | | (792) | | | | | | | | | | (31,881) | | (31,881) | |
| Sales of treasury stock | | 418 | | | (1,295) | | | | | | | 6,941 | | 5,646 | |
| Common shares issued from treasury stock for benefit plans | | 209 | | | 5,238 | | | | | | | 4,097 | | 9,335 | |
| Tax benefit attributable to exercise of stock options | | | | | 3,778 | | | | | | | | | 3,778 | |
| Stock-based compensation | | | | | 6,680 | | | | | | | | | 6,680 | |
| Purchases of stock by deferred compensation plan | | 3 | (4) | | 59 | | | | | 179 | | 49 | (179) | 108 | |
| Distribution of stock from deferred compensation plan | | | 44 | | | | | | | (437) | | | 437 | | |
| Foreign currency translation adjustments | | | | | | (14,018) | | | (14,018) | | | | | (14,018) | |
| Reclassification of unrecognized derivative losses to earnings | | | | | | | 131 | | 131 | | | | | 131 | |
| Minimum retirement benefits liability adjustments | | | | | | | | 141 | 141 | | | | | 141 | |
| Taxes on changes in accumulated other comprehensive earnings | | | | | | 2,127 | (50) | (50) | 2,027 | | | | | 2,027 | |
| Balances as of June 30, 2012 | 72,960 | (4,232) | (275) | \$ 106 | \$ 95,913 | \$ 10,212 | \$ (403) | \$ (17,902) | \$ (8,093) | \$ 4,323 | \$ 1,029,188 | \$ (136,455) | \$ (4,323) | \$ 980,659 | |

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Note 1. Basis of presentation

The Condensed Consolidated Financial Statements of Woodward, Inc. (Woodward or the Company) as of June 30, 2012 and for the three and nine-months ending June 30, 2012 and June 30, 2011, included herein, have not been audited by an independent registered public accounting firm. These Condensed Consolidated Financial Statements reflect all normal recurring adjustments that, in the opinion of management, are necessary to present fairly Woodward's financial position as of June 30, 2012, and the statements of earnings, comprehensive earnings, cash flows, and changes in the statement of stockholders' equity for the periods presented herein. The Condensed Consolidated Balance Sheet as of September 30, 2011 was derived from Woodward's Annual Report on Form 10-K for the fiscal year then ended. The results of operations for the three and nine-months ending June 30, 2012 are not necessarily indicative of the operating results to be expected for other interim periods or for the full fiscal year. Dollar amounts contained in these Condensed Consolidated Financial Statements are in thousands, except per share amounts.

The Condensed Consolidated Financial Statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for interim reporting. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) have been condensed or omitted pursuant to such rules and regulations.

These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in Woodward's most recent Annual Report on Form 10-K filed with the SEC and other financial information filed with the SEC.

Management is required to use estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements, the reported revenues and expenses recognized during the reporting period, and certain financial statement disclosures, in the preparation of the Condensed Consolidated Financial Statements. Significant estimates in these Condensed Consolidated Financial Statements include allowances for losses on receivables, net realizable value of inventories, warranty reserves, timing of recognition on percentage complete on long-term contracts, cost of sales incentives, useful lives of property and identifiable intangible assets, the evaluation of impairments of property, identifiable intangible assets and goodwill, income tax and valuation reserves, the valuation of assets and liabilities acquired in business combinations, assumptions used in the determination of the funded status and annual expense of pension and postretirement employee benefit plans, the valuation of stock compensation instruments granted to employees and board members, and contingencies. Actual results could vary materially from Woodward's estimates.

Woodward serves two significant markets—the aerospace market and the energy market. In order to better serve these markets, Woodward completed a realignment of its reportable segments at September 30, 2011 and now reports its financial results through two reportable segments Aerospace and Energy. The Aerospace segment combines the aircraft propulsion portion of the former Turbine Systems business group, now referred to as the Aircraft Turbine Systems business group, with the Airframe Systems business group. The Energy segment combines the industrial turbine portion of the former Turbine Systems business group, now referred to as the Industrial Turbomachinery Systems business group, with the Engine Systems and Electrical Power Systems business groups.

Prior period information has been revised to be consistent with the Company's current reportable segment structure, which is based upon how it managed its business as of September 30, 2011 and during the first nine months of fiscal year 2012.

Note 2. Recent accounting pronouncements

From time to time, the Financial Accounting Standards Board (FASB) or other standard-setting bodies issue new accounting pronouncements. Updates to the FASB Accounting Standards Codification (ASC) are communicated through issuance of an Accounting Standards Update (ASU).

In September 2011, the FASB issued ASU 2011-08, Testing Goodwill for Impairment. ASU 2011-08 allows companies to perform a qualitative assessment to determine whether or not the current two-step quantitative testing method, in which a company compares the fair value of reporting units to its carrying amount including goodwill, must be followed. If a qualitative assessment indicates that it is more-likely-than-not

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that the fair value of a reporting unit is greater than its carrying amount, then the quantitative impairment test is not required. A company may choose to use the qualitative assessment on none, some, or all of its reporting units or to bypass the qualitative assessment and proceed directly to the two-step quantitative testing method. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011; however, early adoption is permitted. Woodward does not anticipate that the adoption of ASU 2011-08 will have a material impact on Woodward's Condensed Consolidated Financial Statements.

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Basic earnings per share is computed by dividing net earnings available to common stockholders by the weighted-average number of shares of common stock outstanding for the period.

Diluted earnings per share reflects the weighted-average number of shares outstanding after the assumed conversion of all dilutive securities.

The following is a reconciliation of net earnings to basic earnings per share and diluted earnings per share:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|----------------------------------|-----------------------------------------|-------------|----------------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Numerator: | | | | |
| Net earnings | \$ 28,302 | \$ 36,056 | \$ 95,470 | \$ 90,545 |
| Denominator: | | | | |
| Basic shares outstanding | 68,922 | 68,793 | 68,973 | 68,785 |
| Dilutive effect of stock options | 1,397 | 1,373 | 1,473 | 1,370 |
| Diluted shares outstanding | 70,319 | 70,166 | 70,446 | 70,155 |
| Income per common share: | | | | |
| Basic earnings per share | \$ 0.41 | \$ 0.52 | \$ 1.38 | \$ 1.32 |
| Diluted earnings per share | \$ 0.40 | \$ 0.51 | \$ 1.36 | \$ 1.29 |

The following stock option grants were outstanding during the three and nine-months ending June 30, 2012 and 2011, but were excluded from the computation of diluted earnings per share because their inclusion would have been anti-dilutive:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-------------------------------|-----------------------------------------|-------------|----------------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Options | 31 | 678 | 45 | 679 |
| Weighted-average option price | \$ 41.53 | \$ 32.06 | \$ 35.87 | \$ 32.03 |

The weighted-average shares of common stock outstanding for basic and diluted earnings per share included weighted-average treasury stock shares held for deferred compensation obligations of the following:

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| | Three-Months | | Nine-Months Ending | |
|-----------------------------------------------------------------------------------|---------------------|---------------|---------------------------|-----------------|
| | Ending | Ending | June 30, | June 30, |
| | 2012 | 2011 | 2012 | 2011 |
| Weighted-average treasury stock shares held for deferred compensation obligations | 284 | 324 | 299 | 340 |

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 4. Business acquisitions****IDS Acquisition**

During the third quarter of fiscal year 2011, Woodward acquired all of the outstanding stock of Integral Drive Systems AG and its European companies, including their respective holding companies (IDS), and the assets of IDS's business in China (collectively, the IDS Acquisition) for an aggregate cash purchase price of \$48,412 paid to the sellers.

IDS is a developer and manufacturer of innovative power electronic systems predominantly in utility scale wind turbines and photovoltaic power plants. IDS also offers key products for power distribution and marine propulsion systems. In addition to wind turbines and photovoltaic plants, its products are used in offshore oil and gas platforms, energy storage and distribution systems, and a variety of industrial applications. IDS has been integrated into Woodward's Energy segment.

The Company believes the IDS Acquisition expands its presence in wind converter offerings and reduces its time to market with expansion of solar energy, energy storage, and marine drives. Goodwill recorded in connection with the IDS Acquisition, which is not deductible for income tax purposes, represents the estimated value of such future opportunities, the value of potential expansion with new customers, the opportunity to further develop sales opportunities with new and acquired IDS customers, and anticipated synergies expected to be achieved through the integration of IDS into Woodward's Energy segment.

As of June 30, 2012, an amount of \$7,659 paid in connection with the IDS Acquisition was deposited into escrow accounts to secure Woodward's ability to recover any amounts owed to Woodward by the sellers as a result of customary indemnities related to representations and warranties made by the sellers. Funds held in escrow will only be released to the sellers as specified in the related purchase agreements.

The purchase price of the IDS Acquisition is as follows:

| | |
|---------------------------------------|------------------|
| Cash paid to sellers | \$ 48,412 |
| Less cash acquired | (1,251) |
| Total purchase price | 47,161 |
| Less marketable securities acquired | (8,463) |
| Price paid for business assets | \$ 38,698 |

The allocation of the purchase price to the assets acquired and liabilities assumed was finalized as of March 31, 2012. Assets acquired and liabilities assumed in the transaction were recorded at their acquisition date fair values, while transaction costs associated with the acquisition were expensed as incurred. The Company's allocation was based on an evaluation of the appropriate fair values and represents management's best estimate based on available data.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of the IDS Acquisition:

| | |
|--------------------------------------|---------------|
| Current assets | \$ 14,627 |
| Investments in marketable securities | 8,463 |
| Property, plant, and equipment | 1,954 |
| Goodwill | 24,188 |
| Intangible assets | 11,882 |
| Total assets acquired | 61,114 |
| Other current liabilities | 5,505 |
| Warranty accrual | 2,250 |
| Postretirement benefits | 434 |
| Deferred tax liabilities | 2,472 |
| Other tax noncurrent | 3,292 |
| Total liabilities assumed | 13,953 |
| Net assets acquired | \$ 47,161 |

There were no changes to the values of assets acquired and liabilities assumed during the nine-months ending June 30, 2012. The fair value of warranty liabilities assumed represents the estimated costs to provide service for contractual warranty obligations on products sold by IDS and IDS's business in China prior to the IDS Acquisition. The fair value of Other tax noncurrent represents the estimated value of gross unrecognized tax benefits assumed.

In connection with the IDS Acquisition, Woodward acquired various marketable securities, which are not classified as cash equivalents under U.S. GAAP. These marketable securities were sold during the fiscal quarter ended June 30, 2011 and reinvested into cash and cash equivalents consistent with Woodward's internal investment and risk management policies. Losses on the sale of marketable securities were included in Other (income) expense, net in the Condensed Consolidated Statements of Earnings for the fiscal quarter ended June 30, 2011.

Also, in connection with the IDS Acquisition, Woodward assumed the net postretirement benefit obligations of five Swiss statutory retirement plans which are considered to be defined benefit plans under U.S. GAAP.

A summary of the intangible assets acquired, weighted-average useful lives, and amortization methods follows:

| | Amount | Weighted-Average Useful Life | Amortization Method |
|------------------------|----------|------------------------------|---------------------|
| Customer relationships | \$ 3,452 | 9 years | Straight-line |
| Process technology | 7,752 | 8.5 years | Straight-line |

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| | | | |
|-------|-----------|-----------|---------------|
| Other | 678 | 2.5 years | Straight-line |
| Total | \$ 11,882 | 8 years | |

The operating results of the IDS Acquisition are included in Woodward's Consolidated Statements of Earnings and Comprehensive Earnings beginning April 15, 2011. Pro forma financial disclosures have not been presented, as the IDS Acquisition was not significant to Woodward's financial position or results of operations. The Company incurred IDS Acquisition related transaction costs of \$2,396 during the year ending September 30, 2011, which were included in Selling, general and administrative expenses in the Condensed Consolidated Statements of Earnings. No additional IDS Acquisition related transaction costs were incurred in the nine-months ending June 30, 2012.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 5. Financial instruments and fair value measurements**

The estimated fair values of Woodward's financial instruments were as follows:

| | At June 30, 2012 | | At September 30, 2011 | |
|----------------------------------------------|------------------|---------------|-----------------------|---------------|
| | Estimated | | Estimated | |
| | Fair Value | Carrying Cost | Fair Value | Carrying Cost |
| Cash and cash equivalents | \$ 39,903 | \$ 39,903 | \$ 74,539 | \$ 74,539 |
| Investments in deferred compensation program | 7,024 | 7,024 | 5,855 | 5,855 |
| Short-term borrowings | (5,000) | (5,000) | | |
| Long-term debt, including current portion | (461,123) | (408,799) | (482,776) | (425,246) |

The fair values of cash and cash equivalents, which include investments in money market funds and reverse repurchase agreements for the overnight investment of excess cash in U.S. government and government agency obligations, are assumed to be equal to their carrying amounts. Cash and cash equivalents have short-term maturities and market interest rates. Woodward's cash and cash equivalents include funds deposited or invested in the U.S. and overseas that are not insured by the Federal Deposit Insurance Corporation (FDIC). Woodward believes that its deposited and invested funds are held by or invested with credit worthy financial institutions or counterparties.

Investments related to the deferred compensation program used to provide deferred compensation benefits to certain employees are carried at market value.

The fair values of short-term borrowings at variable interest rates are assumed to be equal to their carrying amounts because such borrowings may be repaid or settled for their carrying amounts within a short period of time.

The fair value of long-term debt was estimated based on a model that discounted future principal and interest payments at interest rates available to the Company at the end of the period for similar debt of the same maturity, which is a Level 2 input as defined below. The weighted-average interest rates used to estimate the fair value of long-term debt were as follows:

| | June 30, 2012 | September 30, 2011 |
|------------------------------------------------------------|------------------|-----------------------|
| Weighted-average interest rate used to estimate fair value | 2.4% | 2.6% |

Financial assets and liabilities recorded at fair value in the Condensed Consolidated Balance Sheet are categorized based upon a fair value hierarchy established by U.S. GAAP, which prioritizes the inputs used to measure fair value into the following levels:

Level 1: Inputs based on quoted market prices in active markets for identical assets or liabilities at the measurement date.

Level 2: Quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable and can be corroborated by observable market data.

Level 3: Inputs reflect management's best estimates and assumptions of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the valuation of the instruments.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The table below presents information about Woodward's financial assets that are measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques Woodward utilized to determine such fair value. Woodward had no financial liabilities required to be measured at fair value on a recurring basis as of June 30, 2012 or September 30, 2011.

| | At June 30, 2012 | | | | At September 30, 2011 | | | |
|-----------------------------------|------------------|---------|---------|-----------|-----------------------|---------|---------|-----------|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Financial assets: | | | | | | | | |
| Investments in money market funds | \$ 10,135 | \$ | \$ | \$ 10,135 | \$ 10,823 | \$ | \$ | \$ 10,823 |
| Equity securities | 7,024 | | | 7,024 | 5,855 | | | 5,855 |
| Total financial assets | \$ 17,159 | \$ | \$ | \$ 17,159 | \$ 16,678 | \$ | \$ | \$ 16,678 |

Investments in money market funds: Woodward sometimes invests excess cash in money market funds not insured by the FDIC. Woodward believes that the investments in money market funds are on deposit with creditworthy financial institutions and that the funds are highly liquid. The investments in money market funds are reported at fair value, with realized gains from interest income realized in earnings, and included in Cash and cash equivalents. The fair values of Woodward's investments in money market funds are based on the quoted market prices for the net asset value of the various money market funds.

Equity securities: Woodward holds marketable equity securities, through investments in various mutual funds, related to its deferred compensation program. Based on Woodward's intentions regarding these instruments, marketable equity securities are classified as trading securities. The trading securities are reported at fair value, with realized gains and losses recognized in earnings. The trading securities are included in Other current assets. The fair values of Woodward's trading securities are based on the quoted market prices for the net asset value of the various mutual funds.

Note 6. Derivative instruments and hedging activities

Woodward is exposed to global market risks, including the effect of changes in interest rates, foreign currency exchange rates, changes in certain commodity prices and fluctuations in various producer indices. From time to time, Woodward enters into derivative instruments for risk management purposes only, including derivatives designated as accounting hedges and/or those utilized as economic hedges. Woodward uses interest rate related derivative instruments to manage its exposure to fluctuations of interest rates. Woodward does not enter into or issue derivatives for trading or speculative purposes.

By using derivative and/or hedging instruments to manage its risk exposure, Woodward is subject, from time to time, to credit risk and market risk on those derivative instruments. Credit risk arises from the potential failure of the counterparty to perform under the terms of the derivative and/or hedging instrument. When the fair value of a derivative contract is positive, the counterparty owes Woodward, which creates credit risk for Woodward. Woodward mitigates this credit risk by entering into transactions with only credit worthy counterparties. Market risk arises from the potential adverse effects on the value of derivative and/or hedging instruments that result from a change in interest rates, commodity prices, or foreign currency exchange rates. Woodward mitigates this market risk by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

Derivatives in foreign currency relationships

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Woodward did not enter into any hedging transactions during the three or nine-months ending June 30, 2012 and was not a party to any derivative instruments as of June 30, 2012 or September 30, 2011.

In September 2010, Woodward entered into a foreign currency exchange rate contract to purchase 39,000 for approximately \$52,549 in early December 2010. An unrealized gain of \$579 on this derivative was carried at fair market value in Other current assets as of September 30, 2010. In December 2010, a loss of \$1,033 was realized on the settlement of this forward contract and was recorded in Other (income) expense, net.

The objective of this derivative instrument, which was not designated as an accounting hedge, was to limit the risk of foreign currency exchange rate fluctuations on certain short-term intercompany loan balances.

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WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

The following table discloses the remaining unrecognized gains and losses in Woodward's Condensed Consolidated Balance Sheets associated with terminated derivative instruments that were previously entered into by the Company:

| | June 30, 2012 | September 30, 2011 |
|--------------------------------------------------------|---------------------------------|-----------------------|
| Derivatives designated as hedging instruments | Unrecognized Gain (Loss) | |
| Classified in accumulated other comprehensive earnings | \$ (651) | \$ (781) |
| Classified in current and long-term debt | | 3 |
| | \$ (651) | \$ (778) |

The following tables disclose the impact of derivative instruments on Woodward's Condensed Consolidated Statements of Earnings:

| | Location of (Gain) Loss Recognized in Earnings | Three-Months Ending June 30, 2012 | | | Three-Months Ending June 30, 2011 | | |
|----------------------------------|---------------------------------------------------|--------------------------------------|------------------------------------------------------|-------------------------------------------------------------|-------------------------------------|------------------------------------------------------|-------------------------------------------------------------|
| | | Amount of (Income) Expense | Amount of (Gain) Loss | Amount of (Gain) Loss | Amount of (Income) Expense | Amount of (Gain) Loss | Amount of (Gain) Loss |
| | | Recognized in Earnings | Recognized in Accumulated OCI on Derivative | Reclassified from Accumulated OCI into Earnings | Recognized in Earnings | Recognized in Accumulated OCI on Derivative | Reclassified from Accumulated OCI into Earnings |
| Derivatives in: | | | | | | | |
| Fair value hedging relationships | Interest expense | \$ | \$ | \$ | \$ (17) | \$ | \$ |
| Cash flow hedging relationships | Interest expense | 42 | | 42 | 57 | | 57 |
| | | \$ 42 | \$ | \$ 42 | \$ 40 | \$ | \$ 57 |

| | Location of (Gain) Loss Recognized in Earnings | Nine-Months Ending June 30, 2012 | | | Nine-Months Ending June 30, 2011 | | |
|----------------------------------|---------------------------------------------------|-------------------------------------|------------------------------------------------------|-------------------------------------------------------------|-------------------------------------|------------------------------------------------------|-------------------------------------------------------------|
| | | Amount of (Income) Expense | Amount of (Gain) Loss | Amount of (Gain) Loss | Amount of (Income) Expense | Amount of (Gain) Loss | Amount of (Gain) Loss |
| | | Recognized in Earnings | Recognized in Accumulated OCI on Derivative | Reclassified from Accumulated OCI into Earnings | Recognized in Earnings | Recognized in Accumulated OCI on Derivative | Reclassified from Accumulated OCI into Earnings |
| Derivatives in: | | | | | | | |
| Fair value hedging relationships | Interest expense | \$ (3) | \$ | \$ | \$ (51) | \$ | \$ |
| Cash flow hedging relationships | Interest expense | 130 | | 130 | 172 | | 172 |
| Foreign currency relationships | Other (income) expense | | | | 1,612 | | |

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\$ 127 \$ \$ 130 \$ 1,733 \$ \$ 172

Based on the carrying value of the unrecognized gains and losses on terminated derivative instruments designated as cash flow hedges as of June 30, 2012, Woodward expects to reclassify \$171 of net unrecognized losses on terminated derivative instruments from accumulated other comprehensive earnings to earnings during the next twelve months.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 7. Supplemental statements of cash flows information**

| | Nine-Months Ending June 30, | |
|--------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------|-------------|
| | 2012 | 2011 |
| Interest paid, net of amounts capitalized | \$ 25,011 | \$ 25,596 |
| Income taxes paid | 41,903 | 33,549 |
| Income tax refunds received | 2,841 | 9,269 |
| Non-cash activities: | | |
| Purchases of property, plant and equipment on account | 1,275 | 1,881 |
| Common shares issued from treasury stock for benefit plans (Note 17) | 9,335 | |
| Cashless exercise of stock options | | 1,124 |
| Reduction of accounts receivable and short-term borrowing due to the settlement of accounts receivable previously sold with recourse | | 3,228 |
| Reduction of accounts payable due to the assignment of accounts receivable with recourse | | 570 |
| Reduction to goodwill due to favorable resolution of lease termination recorded in restructuring reserve | | 103 |
| Payment of director fees through issuance of treasury stock | | 38 |

Note 8. Inventories

| | June 30, 2012 | September 30, 2011 |
|------------------------------------|--------------------------|-------------------------------|
| Raw materials | \$ 30,943 | \$ 43,172 |
| Work in progress | 94,112 | 108,718 |
| Component parts and finished goods | 298,939 | 229,665 |
| | \$ 423,994 | \$ 381,555 |

Note 9. Property, plant, and equipment, net

| | June 30, 2012 | September 30, 2011 |
|------------------------------------|--------------------------|-------------------------------|
| Land | \$ 14,422 | \$ 14,823 |
| Buildings and improvements | 191,774 | 177,637 |
| Leasehold improvements | 20,079 | 18,765 |
| Machinery and production equipment | 265,213 | 265,898 |
| Computer equipment and software | 81,018 | 66,149 |
| Other | 25,330 | 25,191 |

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| | | |
|------------------------------------|------------|------------|
| Construction in progress | 39,814 | 44,975 |
| | 637,650 | 613,438 |
| Less accumulated depreciation | (423,504) | (406,713) |
| Property, plant and equipment, net | \$ 214,146 | \$ 206,725 |

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|----------------------|---------------------------------|-----------|--------------------------------|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Depreciation expense | \$ 9,497 | \$ 10,955 | \$ 29,179 | \$ 31,279 |

During fiscal year 2010, Woodward began construction of a new forty-eight thousand square foot system test facility in Rockford, Illinois. In the first nine months of fiscal year 2012, Woodward placed into service assets totaling \$16,738 associated with the new system test facility, the majority of which is included in Buildings and improvements. As of June 30, 2012, \$5,511 of assets related to the system test facility remained as construction in progress and are expected to be placed into service by the end of fiscal year 2012. The facility, which houses numerous environmental system test cells and a vibration lab, will support, among other development projects, Woodward's Aerospace segment development efforts of next generation fuel systems for aircraft turbines.

The increase in Computer equipment and software of \$14,869 was primarily related to assets that were placed into service during the first nine months of fiscal year 2012 associated with a new enterprise resource planning (ERP) system for a group within Woodward's Aerospace segment.

For the three and nine-months ending June 30, 2012 and June 30, 2011, Woodward had capitalized interest that would have otherwise been included in interest expense as follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|----------------------|---------------------------------|--------|--------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Capitalized interest | \$ 147 | \$ 383 | \$ 575 | \$ 896 |

Note 10. Goodwill

| | September 30, 2011 | Effects of Foreign Currency Translation | June 30, 2012 |
|--------------|-----------------------|--------------------------------------------------|---------------|
| | | | |
| Aerospace | \$ 356,525 | \$ 30 | \$ 356,555 |
| Energy | 105,757 | (1,803) | 103,954 |
| Consolidated | \$ 462,282 | \$ (1,773) | \$ 460,509 |

Woodward tests goodwill for impairment at the individual or aggregate reporting unit level, as appropriate, on an annual basis and more often if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The impairment tests consist of comparing the implied fair value of each identified reporting unit with its carrying amount including goodwill. If the carrying amount of the reporting unit exceeds its implied fair value, Woodward compares the implied fair value of goodwill with the recorded carrying amount of goodwill. If the carrying amount of goodwill exceeds the implied fair value of goodwill, an impairment loss would be recognized to reduce the carrying amount to its implied fair value.

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Woodward completed its annual goodwill impairment test as of July 31, 2011 during the quarter ended September 30, 2011. As a part of that test, the fair value of each of Woodward's reporting units was determined using a discounted cash flow method. This method represents a Level 3 input and incorporates various estimates and assumptions, the most significant being projected revenue growth rates, operating earnings margins, and forecasted cash flows based on the discount rate and terminal growth rate. Management projects revenue growth rates, operating earnings margins and cash flows based on each reporting unit's current operational results, expected performance and operational strategies over a five or ten-year period. These projections are adjusted to reflect economic conditions and the demand for certain products and require considerable management judgment.

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WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Forecasted cash flows used in the July 31, 2011 impairment test were discounted using weighted-average cost of capital assumptions from 10.0% to 10.2%. The terminal values of the forecasted cash flows were calculated using the Gordon Growth Model and assumed an annual compound growth rate after five or ten years of 4.3%. These inputs, which are unobservable in the market, represent management's best estimate of what market participants would use in determining the present value of the Company's forecasted cash flows. Changes in these estimates and assumptions can have a significant impact on the fair value of forecasted cash flows. Woodward evaluated the reasonableness of the reporting units resulting fair values utilizing a market multiple method.

The results of Woodward's goodwill impairment tests performed as of July 31, 2011 indicated the estimated fair value of each reporting unit was substantially in excess of its carrying value, and accordingly, no impairment existed.

As part of the Company's ongoing monitoring efforts, Woodward will continue to consider the global economic environment and its potential impact on Woodward's business at a reporting unit level in assessing goodwill recoverability. There can be no assurance that Woodward's estimates and assumptions regarding forecasted cash flows of certain reporting units, the period or strength of the current economic recovery, or the other inputs used in forecasting the present value of forecasted cash flows will prove to be accurate projections of future performance.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 11. Other intangibles, net**

| | June 30, 2012 | | | September 30, 2011 | | |
|--------------------------------|----------------------|--------------------------|---------------------|----------------------|--------------------------|---------------------|
| | Gross Carrying Value | Accumulated Amortization | Net Carrying Amount | Gross Carrying Value | Accumulated Amortization | Net Carrying Amount |
| Customer relationships: | | | | | | |
| Aerospace | \$ 205,177 | \$ (54,880) | \$ 150,297 | \$ 205,171 | \$ (41,652) | \$ 163,519 |
| Energy | 41,711 | (25,857) | 15,854 | 41,991 | (23,696) | 18,295 |
| Total | \$ 246,888 | \$ (80,737) | \$ 166,151 | \$ 247,162 | \$ (65,348) | \$ 181,814 |
| Intellectual property: | | | | | | |
| Aerospace | \$ | \$ | \$ | \$ | \$ | \$ |
| Energy | 19,919 | (12,843) | 7,076 | 20,162 | (11,918) | 8,244 |
| Total | \$ 19,919 | \$ (12,843) | \$ 7,076 | \$ 20,162 | \$ (11,918) | \$ 8,244 |
| Process technology: | | | | | | |
| Aerospace | \$ 71,694 | \$ (19,309) | \$ 52,385 | \$ 71,691 | \$ (15,380) | \$ 56,311 |
| Energy | 23,100 | (9,179) | 13,921 | 23,451 | (7,657) | 15,794 |
| Total | \$ 94,794 | \$ (28,488) | \$ 66,306 | \$ 95,142 | \$ (23,037) | \$ 72,105 |
| Other intangibles: | | | | | | |
| Aerospace | \$ 39,637 | \$ (36,985) | \$ 2,652 | \$ 39,635 | \$ (34,655) | \$ 4,980 |
| Energy | 2,504 | (1,196) | 1,308 | 2,621 | (867) | 1,754 |
| Total | \$ 42,141 | \$ (38,181) | \$ 3,960 | \$ 42,256 | \$ (35,522) | \$ 6,734 |
| Total intangibles: | | | | | | |
| Aerospace | \$ 316,508 | \$ (111,174) | \$ 205,334 | \$ 316,497 | \$ (91,687) | \$ 224,810 |
| Energy | 87,234 | (49,075) | 38,159 | 88,225 | (44,138) | 44,087 |
| Consolidated Total | \$ 403,742 | \$ (160,249) | \$ 243,493 | \$ 404,722 | \$ (135,825) | \$ 268,897 |

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|----------------------|---------------------------------|----------|--------------------------------|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Amortization expense | \$ 8,139 | \$ 8,935 | \$ 24,691 | \$ 26,020 |

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Future amortization expense associated with intangibles is expected to be:

| Year Ending September 30: | |
|----------------------------------|------------|
| 2012 (remaining) | \$ 8,124 |
| 2013 | 30,418 |
| 2014 | 27,270 |
| 2015 | 24,764 |
| 2016 | 23,397 |
| Thereafter | 129,520 |
| | \$ 243,493 |

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WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Note 12. Credit facilities, short-term borrowings and long-term debt

As of December 31, 2011, Woodward had a \$225,000 revolving credit facility related to unsecured financing arrangements with a syndicate of U.S. banks. The revolving credit facility agreement provided for an option to increase available borrowings to \$350,000, subject to the lenders participation, and had an expiration date of October 2012. The interest rate on borrowings under the revolving credit facility agreement varied with LIBOR, the federal funds rate, or the prime rate.

On January 4, 2012, the \$225,000 revolving credit facility was amended and restated by the Third Amended and Restated Credit Agreement (the Amended and Restated Revolver Agreement) entered into between Woodward and a syndicate of nine lenders led by JPMorgan Chase Bank, N.A., as administrative agent. The Amended and Restated Revolver Agreement extended the existing revolving credit facility's maturity to January 2017. The borrowing capacity increased from \$225,000 to \$400,000 and the option, subject to the lenders' participation, to expand the commitment increased from \$125,000 to \$200,000, for a total borrowing capacity of up to \$600,000. Borrowings under the Amended and Restated Revolver Agreement generally bear interest at LIBOR plus 0.95% to 1.525%. There were no outstanding borrowings under the revolving credit facility as of June 30, 2012.

The Amended and Restated Revolver Agreement contains certain covenants customary with such agreements, which are generally consistent with the covenants applicable to Woodward's long-term debt agreements, and contains customary events of default, including certain cross default provisions related to Woodward's other outstanding debt arrangements in excess of \$30,000, the occurrence of which would permit the lenders to accelerate the amounts due thereunder. In addition, the Amended and Restated Revolver Agreement increases the minimum required consolidated net worth of Woodward to a base of \$725,000, plus 50% of Woodward's positive net income for the prior fiscal year and plus 50% of Woodward's net cash proceeds resulting from certain issuances of stock, subject to certain adjustments. Woodward also made amendments to its existing Term Loan Credit Agreement, dated as of October 1, 2008 (the Term Loan Agreement), that provided for certain changes to, among other things, the affirmative, negative and financial covenants of the Term Loan Agreement consistent with the covenant provisions in the Amended and Restated Revolver Agreement.

Woodward's obligations under the Amended and Restated Revolver Agreement and the Term Loan Agreement are guaranteed by Woodward FST, Inc., MPC Products Corporation and Woodward HRT, Inc., each of which is a wholly owned subsidiary of Woodward.

In connection with the Amended and Restated Revolver Agreement, Woodward incurred \$2,185 in financing costs, which were deferred and will be amortized to Interest expense using the straight-line method over the life of the agreement. The remaining \$100 of deferred financing costs incurred in connection with the prior \$225,000 revolving credit facility were expensed in the first quarter of fiscal year 2012 and are included in Interest expense in the Condensed Consolidated Statements of Earnings.

On January 5, 2012, a Chinese subsidiary of Woodward entered into a local credit facility with the Hong Kong and Shanghai Banking Company under which it has the ability to borrow up to either \$5,000, or the local currency equivalent of \$5,000. Any cash borrowings under the local Chinese credit facility are secured by a parent guarantee from Woodward. The Chinese subsidiary may utilize the local facility for cash borrowings to support its local operating cash needs. Local currency borrowings on the Chinese credit facility are charged interest at the prevailing interest rate offered by the People's Bank of China on the date of borrowing, plus a margin equal to 25% of that prevailing rate. U.S. dollar borrowings on the credit facility are charged interest at the lenders cost of borrowing rate at the date of borrowing, plus a margin of 3%.

At June 30, 2012, the Chinese subsidiary had outstanding cash borrowings of \$5,000 which were fully secured by a \$5,000 parent guarantee issued by Woodward. The U.S. dollar borrowings were made at an effective interest rate of 7.45%.

Woodward also has other foreign lines of credit and foreign overdraft facilities at various financial institutions, which are generally reviewed annually for renewal and are subject to the usual terms and conditions applied by the financial institutions. Pursuant to the terms of the related facility agreements, Woodward's foreign performance guarantee facilities are limited in use to providing performance guarantees to third parties.

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As of June 30, 2012 and September 30, 2011, there were no outstanding borrowings from Woodward's other foreign lines of credit and foreign overdraft facilities.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

At June 30, 2012, Woodward held \$39,903 in cash and cash equivalents, and had total outstanding debt of \$413,799 with additional borrowing availability of \$393,667 under its revolving credit facility, net of outstanding letters of credit, and \$14,797 under its other foreign lines of credit and foreign overdraft facilities.

Management believes that Woodward was in compliance with all its debt covenants at June 30, 2012.

Note 13. Accrued liabilities

| | June 30, 2012 | September 30, 2011 |
|----------------------------------------------------|--------------------------|-------------------------------|
| Salaries and other member benefits | \$ 38,843 | \$ 70,965 |
| Current portion of restructuring and other charges | 961 | 2,489 |
| Warranties | 13,979 | 14,083 |
| Interest payable | 5,715 | 11,611 |
| Accrued retirement benefits | 2,555 | 2,560 |
| Deferred revenues | 7,881 | 8,160 |
| Taxes, other than income | 9,833 | 5,097 |
| Other | 18,789 | 18,551 |
| | \$ 98,556 | \$ 133,516 |

Warranties

Provisions of Woodward's sales agreements include product warranties customary to these types of agreements. Accruals are established for specifically identified warranty issues that are probable to result in future costs. Warranty costs are accrued on a non-specific basis whenever past experience indicates a normal and predictable pattern exists. Changes in accrued product warranties were as follows:

| | |
|---------------------------------------------------------------|------------------|
| Warranties, September 30, 2011 | \$ 14,083 |
| Increases to accruals related to warranties during the period | 2,616 |
| Settlements of amounts accrued | (2,308) |
| Foreign currency exchange rate changes | (412) |
| Warranties, June 30, 2012 | \$ 13,979 |

Restructuring and other charges

The main components of accrued non-acquisition related restructuring charges, which were recognized in fiscal year 2009, include workforce management costs associated with the early retirement and the involuntary separation of employees in connection with a strategic realignment of global workforce capacity. Restructuring charges related to fiscal year 2009 business acquisitions include a number of items such as those associated with integrating similar operations, workforce management, vacating certain facilities, and the cancellation of some contracts.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The summary of the activity in accrued restructuring charges during the three and nine-months ending June 30, 2012 is as follows:

| | Three-Months Ending June 30, 2012 | | |
|-----------------------------------------------|----------------------------------------------|----------------------------------|--------------|
| | Restructuring Charges | Business Acquisitions | Total |
| Accrued restructuring charges, March 31, 2012 | \$ 247 | \$ 2,454 | \$ 2,701 |
| Payments | (74) | (45) | (119) |
| Non-cash adjustments | 6 | (516) | (510) |
| Foreign currency exchange rates | (1) | | (1) |
| Accrued restructuring charges, June 30, 2012 | \$ 178 | \$ 1,893 | \$ 2,071 |

| | Nine-Months Ending June 30, 2012 | | |
|---------------------------------------------------|---------------------------------------------|----------------------------------|--------------|
| | Restructuring Charges | Business Acquisitions | Total |
| Accrued restructuring charges, September 30, 2011 | \$ 365 | \$ 2,544 | \$ 2,909 |
| Payments | (204) | (135) | (339) |
| Non-cash adjustments | 18 | (516) | (498) |
| Foreign currency exchange rates | (1) | | (1) |
| Accrued restructuring charges, June 30, 2012 | \$ 178 | \$ 1,893 | \$ 2,071 |

Other liabilities included the following amounts of accrued restructuring charges not expected to be settled within twelve months:

| | June 30, 2012 | September 30, 2011 |
|-------------------------------------------|--------------------------|-------------------------------|
| Non-current accrued restructuring charges | \$ 1,110 | \$ 420 |

Note 14. Other liabilities

| | June 30, 2012 | September 30, 2011 |
|-------------------------------------------------------------------------------------|--------------------------|-------------------------------|
| Net accrued retirement benefits, less amounts recognized within accrued liabilities | \$ 62,205 | \$ 61,994 |
| Uncertain tax positions, net of offsetting benefits (Note 16) | 14,798 | 14,078 |
| Other | 13,586 | 12,622 |

\$ 90,589 \$ 88,694

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 15. Other (income) expense, net**

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-----------------------------------------------------------------------------|---------------------------------|--------|--------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Net (gain) loss on sale of assets | \$ (12) | \$ 428 | \$ (84) | \$ 429 |
| Rent income | (120) | (130) | (376) | (437) |
| Net (gain) loss on investments in deferred compensation program | 150 | (46) | (746) | (614) |
| Net expense recognized in earnings on foreign currency derivatives (Note 6) | | | | 1,612 |
| Other | (6) | (3) | (8) | (35) |
| | \$ 12 | \$ 249 | \$ (1,214) | \$ 955 |

For additional information regarding Net expense recognized in earnings on foreign currency derivatives refer to Note 6, *Derivative instruments and hedging activities*.

Included in the Net (gain) loss on sale of assets for the three and nine-months ending June 30, 2011, is a net loss of \$246 on the sale of the marketable securities acquired in the IDS Acquisition.

Note 16. Income taxes

U.S. GAAP requires that the interim period tax provision be determined as follows:

At the end of each quarter, Woodward estimates the tax that will be provided for the current fiscal year stated as a percentage of estimated ordinary income. The term ordinary income refers to earnings from continuing operations before income taxes, excluding significant unusual or infrequently occurring items.

The estimated annual effective rate is applied to the year-to-date ordinary income at the end of each quarter to compute the estimated year-to-date tax applicable to ordinary income. The tax expense or benefit related to ordinary income in each quarter is the difference between the most recent year-to-date and the prior quarter year-to-date computations.

The tax effects of significant unusual or infrequently occurring items are recognized as discrete items in the interim period in which the events occur. The impact of changes in tax laws or rates on deferred tax amounts, the effects of changes in judgment about beginning of the year valuation allowances, and changes in tax reserves resulting from the finalization of tax audits or reviews are examples of significant unusual or infrequently occurring items that are recognized as discrete items in the interim period in which the event occurs.

The determination of the annual effective tax rate is based upon a number of significant estimates and judgments, including the estimated annual pretax income of Woodward in each tax jurisdiction in which it operates, and the development of tax planning strategies during the year. In addition, as a global commercial enterprise, Woodward's tax expense can be impacted by changes in tax rates or laws, the finalization of tax audits and reviews, changes in the estimate of the amount of undistributed foreign earnings that Woodward considers indefinitely reinvested, as

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well as other factors that cannot be predicted with certainty. As such, there can be significant volatility in interim tax provisions.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The following table sets forth the tax expense and the effective tax rate for Woodward's income from operations:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|------------------------------|---------------------------------|-----------|--------------------------------|------------|
| | 2012 | 2011 | 2012 | 2011 |
| Earnings before income taxes | \$ 37,708 | \$ 50,855 | \$ 131,922 | \$ 128,817 |
| Income tax expense | 9,406 | 14,799 | 36,452 | 38,272 |
| Effective tax rate | 24.9% | 29.1% | 27.6% | 29.7% |

In determining the tax amounts in Woodward's financial statements, estimates are sometimes used that are subsequently adjusted in the actual filing of tax returns or by updated calculations. Such adjustments resulted in a net tax benefit of \$2,592 and \$3,429 in the third quarter and first nine months of fiscal year 2012, respectively. In fiscal year 2011 such adjustments resulted in a net tax benefit of \$1,880 and \$1,607 in the third quarter and first nine months, respectively. In addition, Woodward occasionally has resolutions of tax issues with tax authorities related to prior years due to the conclusion of audits and the lapse of applicable statutes of limitations. Such resolutions resulted in a net tax benefit of \$968 and \$1,130 in the third quarter and first nine months of fiscal year 2012, respectively. In fiscal year 2011, such resolutions resulted in a net tax benefit of \$191 and \$353 in the third quarter and first nine months, respectively.

Income taxes for the nine-months ending June 30, 2012 included a tax benefit of \$3,326 related to a reduction in the anticipated amount of undistributed earnings of certain of Woodward's foreign subsidiaries that were previously expected to be repatriated into the U.S. within the foreseeable future. Woodward now anticipates that a portion of those earnings will remain indefinitely invested outside the U.S. to support the growth of its foreign operations, and has accordingly reversed the deferred tax liability associated with repatriating those earnings.

Income taxes for the nine-months ending June 30, 2011 included an expense reduction of \$3,088 related to the retroactive extension of the U.S. research and experimentation tax credit.

Worldwide unrecognized tax benefits were as follows:

| | June 30, 2012 | September 30, 2011 |
|------------------------------------------------------------------------------------------------------------------|------------------|-----------------------|
| Gross liability | \$ 17,837 | \$ 16,931 |
| Amount that would impact Woodward's effective tax rate, if recognized, net of expected offsetting adjustments | 14,798 | 14,078 |

At this time, Woodward estimates that it is reasonably possible that the liability for unrecognized tax benefits will decrease by as much as \$2,149 in the next twelve months due to the completion of reviews by tax authorities and the expiration of certain statutes of limitations.

Woodward recognizes interest and penalties related to unrecognized tax benefits in tax expense. Woodward had accrued interest and penalties of the following:

| | June 30, 2012 | September 30, 2011 |
|--|------------------|-----------------------|
| | | |

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| | | |
|--------------------------------|----------|----------|
| Accrued interest and penalties | \$ 1,521 | \$ 1,989 |
|--------------------------------|----------|----------|

Woodward's tax returns are audited by U.S., state, and foreign tax authorities, and these audits are at various stages of completion at any given time. Fiscal years remaining open to examination in significant foreign jurisdictions include 2004 and forward. Woodward has been subject to U.S. Federal income tax examinations for fiscal years through 2008. Woodward is subject to U.S. state income tax examinations for fiscal years 2007 and forward.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)***Note 17. Retirement benefits**

Woodward provides various benefits to eligible members of the Company, including contributions to various defined contribution plans, pension benefits associated with defined benefit plans, postretirement medical benefits and postretirement life insurance benefits. Eligibility requirements and benefit levels vary depending on employee location.

Defined contribution plans

Substantially all U.S. employees are eligible to participate in the U.S. defined contribution plan. The U.S. defined contribution plan allows employees to defer part of their annual income for income tax purposes into their personal 401(k) accounts. The Company makes contributions to eligible employee accounts, which are also deferred for employee personal income tax purposes. Certain foreign employees are also eligible to participate in foreign plans.

Most U.S. employees with at least two years of service receive an annual contribution of Woodward stock, equal to 5% of their eligible prior year wages, to their personal Woodward Retirement Savings Plan accounts. In February 2012, Woodward fulfilled the annual Woodward stock contribution obligation using shares held in treasury stock by issuing 209 shares of common stock for a total value of \$9,335. In the second quarter of fiscal year 2011, the annual Woodward stock contribution totaling \$9,107 was funded by way of a cash contribution to the Woodward Retirement Savings Plan, which then purchased shares of Woodward stock on the open market.

The amount of expense associated with defined contribution plans was as follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|---------------|---------------------------------|----------|--------------------------------|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Company costs | \$ 4,866 | \$ 4,174 | \$ 13,848 | \$ 12,430 |

Woodward operates one multi-employer plan for certain employees in the Netherlands. The amounts of contributions associated with the multi-employer plan were as follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-----------------------|---------------------------------|--------|--------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Company contributions | \$ 122 | \$ 121 | \$ 364 | \$ 355 |

Defined benefit plans

Woodward has defined benefit plans that provide pension benefits for certain retired employees in the U.S., the United Kingdom, Japan, and Switzerland. Woodward also provides other postretirement benefits to its employees including postretirement medical benefits and life insurance benefits. Postretirement medical benefits are provided to certain current and retired employees and their covered dependants and beneficiaries in the U.S. and the United Kingdom. Life insurance benefits are provided to certain retirees in the U.S. under frozen plans, which are no longer available to current employees. A September 30 measurement date is utilized to value plan assets and obligations for all of Woodward's defined benefit pension and other postretirement benefit plans.

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U.S. GAAP requires that, for obligations outstanding as of September 30, 2011, the funded status reported in interim periods shall be the same asset or liability recognized in the previous year end statement of financial position adjusted for (a) subsequent accruals of net periodic benefit cost that exclude the amortization of amounts previously recognized in other comprehensive income (for example, subsequent accruals of service cost, interest cost, and return on plan assets) and (b) contributions to a funded plan or benefit payments.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The components of the net periodic retirement pension costs recognized are as follows:

| | United States | | Three-Months Ending June 30, Other Countries | | Total | |
|-------------------------------------------------------|---------------|---------------|-------------------------------------------------|---------------|-----------------|-----------------|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| | Service cost | \$ 883 | \$ 858 | \$ 282 | \$ 273 | \$ 1,165 |
| Interest cost | 1,454 | 1,412 | 571 | 584 | 2,025 | 1,996 |
| Expected return on plan assets | (1,752) | (1,673) | (646) | (649) | (2,398) | (2,322) |
| Amortization of: | | | | | | |
| Net actuarial (gain) loss | 131 | 78 | 167 | 227 | 298 | 305 |
| Prior service cost (benefit) | 19 | 19 | (3) | (2) | 16 | 17 |
| Net periodic retirement pension (benefit) cost | \$ 735 | \$ 694 | \$ 371 | \$ 433 | \$ 1,106 | \$ 1,127 |
| Contributions paid | \$ 150 | \$ 1,290 | \$ 457 | \$ 502 | \$ 607 | \$ 1,792 |

| | United States | | Nine-Months Ending June 30, Other Countries | | Total | |
|-------------------------------------------------------|-----------------|-----------------|------------------------------------------------|-----------------|-----------------|-----------------|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| | Service cost | \$ 2,648 | \$ 2,575 | \$ 854 | \$ 719 | \$ 3,502 |
| Interest cost | 4,362 | 4,235 | 1,709 | 1,701 | 6,071 | 5,936 |
| Expected return on plan assets | (5,256) | (5,020) | (1,936) | (1,895) | (7,192) | (6,915) |
| Amortization of: | | | | | | |
| Net actuarial (gain) loss | 393 | 234 | 499 | 672 | 892 | 906 |
| Prior service cost (benefit) | 56 | 56 | (7) | (6) | 49 | 50 |
| Net periodic retirement pension (benefit) cost | \$ 2,203 | \$ 2,080 | \$ 1,119 | \$ 1,191 | \$ 3,322 | \$ 3,271 |
| Contributions paid | \$ 450 | \$ 1,290 | \$ 2,789 | \$ 3,692 | \$ 3,239 | \$ 4,982 |

The components of the net periodic other postretirement benefit costs recognized are as follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|------------------------------|---------------------------------|-------|--------------------------------|-------|
| | 2012 | 2011 | 2012 | 2011 |
| | Service cost | \$ 17 | \$ 23 | \$ 52 |
| Interest cost | 449 | 494 | 1,348 | 1,481 |
| Amortization of: | | | | |
| Net actuarial (gain) loss | 22 | 32 | 68 | 96 |
| Prior service cost (benefit) | (137) | (218) | (412) | (653) |

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| | | | | |
|--------------------------------------------------|--------|--------|----------|----------|
| Net periodic other postretirement (benefit) cost | \$ 351 | \$ 331 | \$ 1,056 | \$ 993 |
| Contributions paid | \$ 673 | \$ 879 | \$ 1,966 | \$ 2,473 |

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The amount of cash contributions made to these plans in any year is dependent upon a number of factors, including minimum funding requirements in the jurisdictions in which Woodward operates and arrangements made with trustees of certain foreign plans. As a result, the actual funding in fiscal year 2012 may differ from the current estimate. Woodward estimates its remaining cash contributions in fiscal year 2012 will be as follows:

| | |
|-------------------------------|--------|
| Retirement pension benefits: | |
| United States | \$ 150 |
| United Kingdom | 407 |
| Japan | |
| Switzerland | 191 |
| Other postretirement benefits | 2,744 |

Note 18. Stock-based compensation**Stock options**

Woodward's 2006 Omnibus Incentive Plan (the "2006 Plan"), which has been approved by Woodward's stockholders, provides for the grant of up to 7,410 stock options to its employees and directors. Woodward believes that these awards align the interest of its employees with those of its stockholders. Stock option awards are granted with an exercise price equal to the market price of Woodward's stock at the date of grant, and generally with a four-year vesting schedule at a vesting rate of 25% per year and a term of 10 years.

The fair value of options granted was estimated on the date of grant using the Black-Scholes-Merton option-valuation model using the assumptions in the following table. Woodward calculates the expected term, which represents the period of time that stock options granted are expected to be outstanding, based upon historical experience of plan participants. Expected volatility is based on historical volatility using daily stock price observations. The estimated dividend yield is based upon Woodward's historical dividend practice and the market value of its common stock. The risk-free rate is based on the U.S. treasury yield curve, for periods within the contractual life of the stock option, at the time of grant.

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|--------------------------|---------------------------------|-----------|--------------------------------|-----------------|
| | 2012 | 2011 | 2012 | 2011 |
| Expected term | 5.9 years | 5.8 years | 5.9 - 8.5 years | 5.8 - 8.7 years |
| Estimated volatility | 55.5% | 53.7% | 48.9% - 55.6% | 48.0% - 54.0% |
| Estimated dividend yield | 0.7% | 1.0% | 0.7% - 1.1% | 1.0% - 1.3% |
| Risk-free interest rate | 1.3% | 1.8% | 1.0% - 1.6% | 1.8% - 2.6% |

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

The following is a summary of the activity for stock option awards during the three and nine-months ending June 30, 2012:

| | Three-Months Ending June 30, 2012 | | Nine-Months Ending June 30, 2012 | |
|----------------------------|--------------------------------------|--------------------------------------------------------|-------------------------------------|--------------------------------------------------------|
| | Number of options | Weighted- Average Exercise Price per Share | Number of options | Weighted- Average Exercise Price per Share |
| Options, beginning balance | 4,673 | \$ 21.76 | 4,228 | \$ 20.12 |
| Options granted | 4 | 42.94 | 849 | 26.10 |
| Options exercised | (28) | 22.71 | (418) | 13.52 |
| Options forfeited | (44) | 27.38 | (54) | 27.23 |
| Options, ending balance | 4,605 | \$ 21.73 | 4,605 | \$ 21.73 |

Changes in non-vested stock options during the three and nine-months ending June 30, 2012 were as follows:

| | Three-Months Ending June 30, 2012 | | Nine-Months Ending June 30, 2012 | |
|----------------------------|--------------------------------------|--------------------------------------------------------|-------------------------------------|--------------------------------------------------------|
| | Number of options | Weighted- Average Exercise Price per Share | Number of options | Weighted- Average Exercise Price per Share |
| Options, beginning balance | 1,729 | \$ 26.99 | 1,368 | \$ 27.71 |
| Options granted | 4 | 42.94 | 849 | 26.10 |
| Options vested | (7) | 28.64 | (483) | 27.44 |
| Options forfeited | (43) | 27.38 | (51) | 27.24 |
| Options, ending balance | 1,683 | \$ 27.02 | 1,683 | \$ 27.02 |

As of June 30, 2012, there was approximately \$12,000 of total unrecognized compensation cost, which assumes a weighted-average forfeiture rate of 6.4%, related to non-vested stock-based compensation arrangements granted under the 2002 Stock Option Plan (for which no further grants will be made) and the 2006 Plan. The remaining unrecognized compensation cost is expected to be recognized over a weighted-average period of approximately 2.6 years.

Information about stock options that have vested, or are expected to vest, and are exercisable at June 30, 2012 was as follows:

| | Number | Weighted- Average Exercise Price | Weighted- Average Remaining Life in Years | Aggregate Intrinsic Value |
|-------------------------------------|--------|----------------------------------------|----------------------------------------------------|---------------------------------|
| Options outstanding | 4,605 | \$ 21.73 | 5.8 | \$ 81,663 |
| Options vested and exercisable | 2,921 | 18.68 | 4.2 | 60,659 |
| Options vested and expected to vest | 4,465 | 21.55 | 5.7 | 79,984 |

Note 19. Commitments and contingencies

Woodward is currently involved in claims, pending or threatened litigation, other legal proceedings, investigations and/or regulatory proceedings arising in the normal course of business, including, among others, those relating to product liability claims, employment matters, workman's compensation claims, contractual disputes, product warranty claims and alleged violations of various laws and regulations. Woodward has accrued for individual matters that it believes are likely to result in a loss when ultimately resolved using estimates of the most likely amount of loss. Legal costs are expensed as incurred and are classified in Selling, general and administrative expenses on the Condensed Consolidated Statements of Earnings.

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WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Woodward is partially self-insured in the U.S. for healthcare and workman's compensation up to predetermined amounts, above which third party insurance applies. Management regularly reviews the probable outcome of these claims and proceedings, the expenses expected to be incurred, the availability and limits of the insurance coverage, and the established accruals for liabilities.

While the outcome of pending claims, proceedings and investigations cannot be predicted with certainty, management believes that any liabilities that may result from these claims, proceedings and investigations will not have a material effect on Woodward's liquidity, financial condition, or results of operations.

In connection with the sale of the Fuel & Pneumatics product line during fiscal year 2009, Woodward assigned to a subsidiary of the purchaser its rights and responsibilities related to certain contracts with the U.S. Government. Woodward provided to the U.S. Government a customary guarantee of the purchaser's subsidiary's obligations under the contracts. The purchaser and its affiliates have agreed to indemnify Woodward for any liability incurred with respect to the guarantee.

In the event of a change in control of Woodward, as defined in change-in-control agreements with its current corporate officers, Woodward may be required to pay termination benefits to such officers.

Note 20. Segment information

Woodward serves two significant markets – the aerospace market and the energy market. In order to better serve these markets, Woodward completed a realignment of its reportable segments in September 2011 and now reports its financial results through two reportable segments Aerospace and Energy. The Aerospace segment combines the aircraft propulsion portion of the former Turbine Systems business group, now referred to as the Aircraft Turbine Systems business group, with the Airframe Systems business group. The Energy segment combines the industrial turbine portion of the former Turbine Systems business group, now referred to as the Industrial Turbomachinery Systems business group, with the Engine Systems and Electrical Power Systems business groups.

Woodward uses reportable segment information internally to manage its business, including the assessment of business segment performance and decisions for the allocation of resources between segments.

The accounting policies of the reportable segments are the same as those of the Company. Woodward evaluates segment profit or loss based on internal performance measures for each segment in a given period. In connection with that assessment, Woodward excludes matters such as charges for restructuring costs, interest income and expense, and certain gains and losses from asset dispositions.

Table of Contents**WOODWARD, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS***(In thousands, except per share amounts)**(Unaudited)*

A summary of consolidated net sales and earnings by segment follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-------------------------------------------|---------------------------------|------------|--------------------------------|--------------|
| | 2012 | 2011 | 2012 | 2011 |
| Segment external net sales: | | | | |
| Aerospace | \$ 214,474 | \$ 215,242 | \$ 632,037 | \$ 601,331 |
| Energy | 245,767 | 223,225 | 704,893 | 621,077 |
| Total consolidated net sales | \$ 460,241 | \$ 438,467 | \$ 1,336,930 | \$ 1,222,408 |
| Segment earnings: | | | | |
| Aerospace | \$ 21,536 | \$ 35,402 | \$ 82,277 | \$ 88,557 |
| Energy | 31,205 | 29,251 | 92,264 | 80,695 |
| Total segment earnings | 52,741 | 64,653 | 174,541 | 169,252 |
| Nonsegment expenses | (8,687) | (7,554) | (23,623) | (21,599) |
| Interest expense, net | (6,346) | (6,244) | (18,996) | (18,836) |
| Consolidated earnings before income taxes | \$ 37,708 | \$ 50,855 | \$ 131,922 | \$ 128,817 |

Segment assets consist of accounts receivable, inventories, property, plant and equipment, net, goodwill, and other intangibles, net. A summary of consolidated total assets by segment follows:

| | June 30, 2012 | September 30, 2011 |
|----------------------------------------------------------|------------------|-----------------------|
| Segment assets: | | |
| Aerospace | \$ 1,042,807 | \$ 1,036,797 |
| Energy | 585,470 | 569,929 |
| Total segment assets | 1,628,277 | 1,606,726 |
| Unallocated corporate property, plant and equipment, net | 12,587 | 8,556 |
| Other unallocated assets | 153,373 | 166,152 |
| Consolidated total assets | \$ 1,794,237 | \$ 1,781,434 |

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
(Amounts in thousands, except per share amounts)

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements regarding future events and our future results within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact are statements that are deemed forward-looking statements. These statements are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of management. Words such as anticipate, believe, estimate, seek, goal, expect, forecast, intend, continue, outlook, plan, project, target, strive, can, could, may, should, will, would, variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characteristics of future events or circumstances are forward-looking statements. Forward-looking statements may include, among others, statements relating to:

future sales, earnings, cash flow, uses of cash, and other measures of financial performance;

description of our plans and expectations for future operations;

the effect of economic downturns or growth in particular regions;

the effect of changes in the level of activity in particular industries or markets;

the availability and cost of materials, components, services, and supplies;

the scope, nature, or impact of acquisition activity and integration into our businesses;

the development, production, and support of advanced technologies and new products and services;

new business opportunities;

restructuring costs and savings;

our plans, objectives, expectations and intentions with respect to recent acquisitions and expected business opportunities that may be available to us;

the outcome of contingencies;

future repurchases of common stock;

future levels of indebtedness and capital spending; and

pension plan assumptions and future contributions.

Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict, including:

a decline in business with, or financial distress of, our significant customers;

the instability in the financial markets, sovereign credit rating downgrades and uncertainty surrounding European sovereign and other debt defaults, and prolonged unfavorable economic and other industry conditions;

our ability to obtain financing, on acceptable terms or at all, to implement our business plans, complete acquisitions, or otherwise take advantage of business opportunities or respond to business pressures;

the long sales cycle, customer evaluation process, and implementation period of some of our products and services;

our ability to implement, and realize the intended effects of, our restructuring efforts;

our ability to successfully manage competitive factors, including prices, promotional incentives, industry consolidation, and commodity and other input cost increases;

our ability to manage our expenses and product mix while responding to sales increases or decreases;

the ability of our subcontractors to perform contractual obligations and our suppliers to provide us with materials of sufficient quality or quantity required to meet our production needs at favorable prices or at all;

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the success of, or expenses associated with, our product development activities;

our ability to integrate acquisitions and manage costs related thereto;

our debt obligations, our debt service requirements, and our ability to operate our business, pursue business strategies and incur additional debt in light of covenants contained in our outstanding debt agreements;

risks related to our U. S. Government contracting activities;

a significant reduction in defense sales due to decreases in the amount of U.S. Federal defense spending, including as a result of the sequestration of appropriations in fiscal year 2013 under the Budget Act or other specific budget cuts impacting defense programs on which we participate;

future impairment charges resulting from changes in the estimates of fair value of reporting units or of long-lived assets;

future subsidiary results or changes in domestic or international tax statutes;

environmental liabilities related to manufacturing activities;

our continued access to a stable workforce and favorable labor relations with our employees;

the geographical location of a significant portion of our Aerospace business in California, which historically has been susceptible to natural disasters;

our ability to successfully manage regulatory, tax, and legal matters (including product liability, patent, and intellectual property matters);

liabilities resulting from legal and regulatory proceedings, inquiries, or investigations by private or U.S. Government persons or entities;

risks from operating internationally, including the impact on reported earnings from fluctuations in foreign currency exchange rates, and changes in the legal and regulatory environments of countries in which we operate;

fair value of defined benefit plan assets and assumptions used in determining our retirement pension and other postretirement benefit obligations and related expenses including, among others, discount rates and investment return on pension assets; and

certain provisions of our charter documents and Delaware law that could discourage or prevent others from acquiring our company.

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These factors are representative of the risks, uncertainties, and assumptions that could cause actual outcomes and results to differ materially from what is expressed or forecast in our forward-looking statements. Other factors are discussed under Risk Factors in our Securities and Exchange Commission (SEC) filings and are incorporated herein by reference.

Therefore, actual results could differ materially and adversely from those expressed in any forward-looking statements. For additional information regarding factors that may affect our actual financial condition and results of operations, see the information under the caption Risk Factors in Part I, Item 1A in our most recent Annual Report on Form 10-K filed with the SEC (our Form 10-K). We undertake no obligation to revise or update any forward-looking statements for any reason.

Unless we have indicated otherwise or the context otherwise requires, references in this Quarterly Report on Form 10-Q to Woodward, the Company, we, us, and our refer to Woodward, Inc. and its consolidated subsidiaries.

Except where we have otherwise indicated or the context otherwise requires, amounts presented in this Quarterly Report on Form 10-Q are in thousands except per share amounts.

This discussion should be read together with Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of our most recent Form 10-K and the Condensed Consolidated Financial Statements and Notes included therein and in this report.

Table of Contents**Non-U.S. GAAP Financial Measures**

Earnings before interest and taxes (EBIT), earnings before interest, taxes, depreciation and amortization (EBITDA) and free cash flow are financial measures not prepared and presented in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Management uses EBIT to evaluate Woodward 's performance without financing and tax related considerations, as these elements may not fluctuate with operating results. Management uses EBITDA in evaluating Woodward 's operating performance, making business decisions, including developing budgets, managing expenditures and forecasting future periods, and evaluating capital structure impacts of various strategic scenarios. Management uses free cash flow, which is defined as net cash flows provided by operating activities less payments for property, plant and equipment, in reviewing the financial performance of Woodward 's various business groups and evaluating cash levels. Securities analysts, investors, and others frequently use EBIT, EBITDA and free cash flow in their evaluation of companies, particularly those with significant property, plant, and equipment, and intangible assets that are subject to amortization. The use of these non-U.S. GAAP financial measures is not intended to be considered in isolation of, or as a substitute for, the financial information prepared and presented in accordance with U.S. GAAP. As EBIT and EBITDA exclude certain financial information compared with net earnings, the most comparable U.S. GAAP financial measure, users of this financial information should consider the information that is excluded. Free cash flow does not necessarily represent funds available for discretionary use and is not necessarily a measure of our ability to fund our cash needs. Our calculations of EBIT, EBITDA and free cash flow may differ from similarly titled measures used by other companies, limiting their usefulness as comparative measures.

EBIT and EBITDA for the three and nine-months ending June 30, 2012 and June 30, 2011 were as follows:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-----------------------------------|---------------------------------|------------------|--------------------------------|-------------------|
| | 2012 | 2011 | 2012 | 2011 |
| Net earnings | \$ 28,302 | \$ 36,056 | \$ 95,470 | \$ 90,545 |
| Income taxes | 9,406 | 14,799 | 36,452 | 38,272 |
| Interest expense | 6,611 | 6,361 | 19,471 | 19,161 |
| Interest income | (265) | (117) | (475) | (325) |
| EBIT | 44,054 | 57,099 | 150,918 | 147,653 |
| Amortization of intangible assets | 8,139 | 8,935 | 24,691 | 26,020 |
| Depreciation expense | 9,497 | 10,955 | 29,179 | 31,279 |
| EBITDA | \$ 61,690 | \$ 76,989 | \$ 204,788 | \$ 204,952 |

Free cash flow for the nine-months ending June 30, 2012 and June 30, 2011 was as follows:

| | Nine-Months Ending June 30, | |
|--------------------------------------------|--------------------------------|------------------|
| | 2012 | 2011 |
| Net cash provided by operating activities | \$ 63,653 | \$ 46,800 |
| Payments for property, plant and equipment | (44,224) | (32,640) |
| Free cash flow | \$ 19,429 | \$ 14,160 |

OVERVIEW**Operational Highlights****Quarterly Highlights**

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Net sales for the third quarter of fiscal 2012 were \$460,241, an increase of 5.0% from \$438,467 for the third quarter of the prior fiscal year. Net sales growth as compared to the third quarter of fiscal 2011 was primarily driven by our Energy segment, reflecting strength in control systems for wind turbines and natural gas systems. Aerospace segment sales in the third quarter were largely consistent when compared to the same quarter of the prior year. Commercial original equipment manufacturer (OEM) and aftermarket sales improved over the same quarter of the prior year, although lower defense sales largely offset these increases in the third quarter of fiscal 2012.

Sequentially, net sales for the third quarter of fiscal 2012 decreased by \$8,552, or 1.8%, to \$460,241 from \$468,793 in the second quarter of fiscal 2012. Aerospace segment sales for the third quarter decreased by \$9,863 or 4.4% when compared to the second quarter of fiscal 2012 due to lower aftermarket sales. Energy segment sales for the third quarter of fiscal 2012 increased \$1,311 or 1.0% from the second quarter of fiscal 2012.

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EBIT for the third quarter of fiscal 2012 was \$44,054, down 22.8% from \$57,099 in the same period of fiscal 2011. The current quarter EBIT was negatively impacted by increased investment in both product development and improved production processes as a result of our being awarded a substantial number of significant new system programs, partially offset by the increased sales volume. Research and development costs increased by \$9,685, or 33.1%, compared to the same quarter of fiscal 2011, reflecting increased investment in awarded new system programs. Variable compensation expense for the third quarter of fiscal 2012 was largely consistent with the third quarter of fiscal 2011.

Net earnings for the third quarter of fiscal 2012 were \$28,302, or \$0.40 per diluted share, compared to \$36,056, or \$0.51 per diluted share, for the third quarter of fiscal 2011. The effective tax rate in the third quarter of fiscal 2012 was 24.9% compared to 29.1% for the third quarter of the prior year.

Year to Date Highlights

Net sales for the first nine months of fiscal 2012 were \$1,336,930, an increase of 9.4% from \$1,222,408 for the first nine months of the prior fiscal year. The sales increase was across both of our segments and reflected continued market share gains and consistent growth in most of the markets we serve.

EBIT for the first nine months of fiscal 2012 was \$150,918, up 2.2% from \$147,653 in the same period of fiscal 2011. Current year EBIT was positively affected by increased sales volumes and favorable price and sales mix, partially offset by increased investment in research and development and improved production processes. Research and development costs increased by \$27,136, or 33.9%, compared to the first nine months of fiscal 2011, reflecting increased investment in awarded new system programs. In addition, variable compensation expense for the first nine months of fiscal 2012 decreased by \$5,883 from the first nine months of fiscal 2011.

Net earnings for the first nine months of fiscal 2012 were \$95,470, or \$1.36 per diluted share, compared to \$90,545, or \$1.29 per diluted share, for the first nine months of fiscal 2011. The effective tax rate in the first nine months of fiscal 2012 was 27.6% compared to 29.7% for the first nine months of the prior year.

Liquidity Highlights

Net cash provided by operating activities for the first nine months of fiscal 2012 was \$63,653 compared to \$46,800 for the same period of fiscal 2011. The increase was primarily attributable to changes in inventory, which utilized \$46,918 of cash in the first nine months of fiscal 2012 compared to \$77,389 of cash utilized in the first nine months of fiscal 2011.

Free cash flow for the first nine months of fiscal 2012 was \$19,429 compared to free cash flow of \$14,160 for the same period of fiscal 2011, due primarily to a reduction of cash utilization for inventory, partially offset by our continuing investment in capital expenditures. EBITDA was consistent with the prior year at \$204,788 for the first nine months of fiscal 2012 compared to \$204,952 for the same period of fiscal 2011. The increase in EBITDA was positively impacted by increased net earnings, offset by decreases in tax, amortization and depreciation expense.

On January 4, 2012, we amended and restated our revolving credit facility, which had an expiration date of October 2012, by entering into a Third Amended and Restated Credit Agreement (the Amended and Restated Revolver Agreement) with a syndicate of lenders led by JPMorgan Chase Bank, N.A., as administrative agent. The Amended and Restated Revolver Agreement extended the prior revolving credit facility's maturity to January 2017. The borrowing capacity increased from \$225,000 to \$400,000 and the option, subject to the lenders' participation, to expand the commitment increased from \$125,000 to \$200,000, for a total borrowing capacity of up to \$600,000.

At June 30, 2012, we held \$39,903 in cash and cash equivalents, and had total outstanding debt of \$413,799 with additional borrowing availability of \$393,667 under our revolving credit facility, net of outstanding letters of credit, and \$14,797 under various foreign credit facilities.

Table of Contents**RESULTS OF OPERATIONS**

The following table sets forth selected consolidated statements of earnings data as a percentage of net sales for each period indicated:

| | Three-Months Ending | | | | Nine-Months Ending | | | |
|-----------------------------------------------|---------------------|-------------------|------------------|----------------------|--------------------|-------------------|------------------|----------------------|
| | June 30, 2012 | % of Net Sales | June 30, 2011 | % of Net Sales | June 30, 2012 | % of Net Sales | June 30, 2011 | % of Net Sales |
| Net sales | \$ 460,241 | 100% | \$ 438,467 | 100% | \$ 1,336,930 | 100% | \$ 1,222,408 | 100% |
| Costs and expenses: | | | | | | | | |
| Cost of goods sold | 329,451 | 71.6 | 304,441 | 69.4 | 936,354 | 70.0 | 858,138 | 70.2 |
| Selling, general, and administrative expenses | 39,627 | 8.6 | 38,470 | 8.8 | 118,984 | 8.9 | 109,581 | 9.0 |
| Research and development costs | 38,958 | 8.5 | 29,273 | 6.7 | 107,197 | 8.0 | 80,061 | 6.5 |
| Amortization of intangible assets | 8,139 | 1.8 | 8,935 | 2.0 | 24,691 | 1.8 | 26,020 | 2.1 |
| Interest expense | 6,611 | 1.4 | 6,361 | 1.5 | 19,471 | 1.5 | 19,161 | 1.6 |
| Interest income | (265) | 0.1 | (117) | 0.0 | (475) | 0.0 | (325) | 0.0 |
| Other (income) expense, net | 12 | 0.0 | 249 | 0.1 | (1,214) | (0.1) | 955 | 0.1 |
| Total costs and expenses | 422,533 | 91.8 | 387,612 | 88.4 | 1,205,008 | 90.1 | 1,093,591 | 89.5 |
| Earnings before income taxes | 37,708 | 8.2 | 50,855 | 11.6 | 131,922 | 9.9 | 128,817 | 10.5 |
| Income tax expense | 9,406 | 2.0 | 14,799 | 3.4 | 36,452 | 2.7 | 38,272 | 3.1 |
| Net earnings | \$ 28,302 | 6.1 | \$ 36,056 | 8.2 | \$ 95,470 | 7.1 | \$ 90,545 | 7.4 |

Other select financial data:

| | June 30, 2012 | September 30, 2011 |
|----------------------------|------------------|-----------------------|
| Working capital | \$ 616,047 | \$ 536,936 |
| Short-term borrowings | 5,000 | |
| Total debt | 413,799 | 425,249 |
| Total stockholders' equity | 980,659 | 919,097 |

Net Sales

Consolidated net sales for the third quarter and first nine months of fiscal 2012 increased by \$21,774, or 5.0%, and \$114,522, or 9.4%, respectively, compared to the same periods of fiscal 2011. Details of the changes in consolidated net sales are as follows:

| | Three-Month Period | Nine-Month Period |
|------------------------------------------------------------|-----------------------|----------------------|
| Consolidated net sales for the period ending June 30, 2011 | \$ 438,467 | \$ 1,222,408 |
| Aerospace volume changes | (5,492) | 16,817 |
| Energy volume changes | 30,289 | 93,355 |
| Price changes | 5,107 | 14,995 |
| Effects of changes in foreign currency rates | (8,130) | (10,645) |
| Consolidated net sales for the period ending June 30, 2012 | \$ 460,241 | \$ 1,336,930 |

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The increase in net sales for the third quarter and first nine months of fiscal 2012 was primarily attributable to sales volume increases in our Energy segment. Control systems for wind turbines, large and small engine markets utilizing natural gas and industrial gas turbines were leading contributors to increased sales in our Energy segment for the third quarter and first nine months of fiscal 2012. Aerospace segment sales in the third quarter were largely consistent when compared to the same quarter of the prior year. Commercial OEM and aftermarket sales improved over the prior year, although lower defense sales largely offset these increases in the third quarter of fiscal 2012. Increased sales during the first nine months of fiscal 2012 in our Aerospace segment were primarily attributable to strong aftermarket and commercial OEM sales.

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Price changes: Increases in selling prices were driven primarily by price increases related to both OEM and aftermarket sales within our Aerospace segment. Selling prices in the Energy segment were relatively unchanged from the prior year, consistent with prevailing market conditions.

Foreign currency exchange rates: During the third quarter and first nine months of fiscal 2012, our net sales were negatively impacted by \$8,130 and \$10,645, respectively, due to changes in foreign currency exchange rates compared to the same periods of fiscal 2011.

Our worldwide sales activities are primarily denominated in U.S. Dollars (USD), European Monetary Units (the Euro), Great Britain Pounds (GBP), Japanese Yen (JPY), and Chinese Yuan (CNY). As the USD, Euro, GBP, JPY, and CNY fluctuate against each other and other currencies, we are exposed to gains or losses on sales transactions. If the CNY, which the Chinese government has not historically allowed to fluctuate significantly against USD, is allowed to fluctuate against USD in the future, we would be exposed to gains or losses on sales transactions denominated in CNY. For additional information on foreign currency exchange rate risk please refer to the risks summarized under the caption Risk Factors in Part I, Item 1A of our most recent Form 10-K.

Costs and Expenses

Cost of goods sold increased by \$25,010 to \$329,451 for the third quarter of fiscal 2012 from \$304,441 for the third quarter of fiscal 2011. Cost of goods sold increased by \$78,216 to \$936,354 for the first nine months of fiscal 2012 from \$858,138 for the first nine months of 2011. Gross margin (as measured by net sales less cost of goods sold, divided by net sales) decreased to 28.4% for the third quarter of fiscal 2012 compared to 30.6% for the same period of the prior year. The decrease in gross margin is primarily due to our increased investment in both product development and improved production processes resulting from our being awarded a substantial number of significant new system programs, which more than offset the favorable prices and sales mix realized by our Aerospace segment. Gross margin of 30.0% for the first nine months of fiscal 2012 was consistent with the same period of the prior year's gross margin of 29.8%.

Selling, general, and administrative expenses increased by \$1,157, or 3.0%, to \$39,627 for the third quarter of fiscal 2012 as compared to \$38,470 for the same period of fiscal 2011. Selling, general and administrative expenses decreased as a percentage of net sales to 8.6% for the third quarter of fiscal 2012 as compared to 8.8% for the same period of fiscal 2011. Selling, general, and administrative expenses increased by \$9,403, or 8.6%, to \$118,984 for the first nine months of fiscal 2012 as compared to \$109,581 for the same period of fiscal 2011. Selling, general, and administrative expenses as a percentage of net sales decreased slightly to 8.9% for the first nine months of fiscal 2012 compared to 9.0% for the first nine months of fiscal 2011. The increase in selling, general and administrative expenses in both comparable periods is due to increases in costs to support our current operations and anticipated sales growth.

Research and development costs increased by \$9,685, or 33.1%, to \$38,958 for the third quarter of fiscal 2012 as compared to \$29,273, for the same period of fiscal 2011. Research and development costs increased by \$27,136, or 33.9%, to \$107,197 for the first nine months of fiscal 2012 as compared to \$80,061 for the same period of fiscal 2011. Research and development costs increased as a percentage of sales to 8.5% and 8.0% for the third quarter and first nine months of fiscal 2012, respectively, as compared to 6.7% and 6.5% for the same respective periods of fiscal 2011. The increase in research and development costs is due to increased investment, particularly within our Aerospace segment, in product development, resulting from our being awarded a substantial number of significant new system programs. Research and development also increased due to market share gains in most of our markets. Our research and development activities extend across nearly all of our customer base.

Amortization of intangible assets decreased slightly to \$8,139 and \$24,691 for the third quarter and first nine months of fiscal 2012, respectively, compared to \$8,935 and \$26,020 for the same periods in fiscal 2011. As a percentage of net sales, amortization of intangible assets decreased to 1.8% for both the third quarter and first nine months of fiscal 2012, respectively, as compared to 2.0% and 2.1% for the same periods of the prior year.

Interest expense increased slightly to \$6,611 and \$19,471 for the third quarter and first nine months of fiscal 2012, respectively, compared to \$6,361 and \$19,161 for the same periods in fiscal 2011. These increases are primarily due to increased average short-term borrowings as compared to the prior year. As a percentage of net sales, interest expense decreased to 1.4% and 1.5% for the third quarter and first nine months of fiscal 2012, respectively, from 1.5% and 1.6% for the same periods of the prior year.

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Income taxes were provided at an effective rate on earnings before income taxes of 24.9% and 27.6% for the third quarter and first nine months of fiscal 2012, respectively, compared to 29.1% and 29.7% for the same periods of fiscal 2011. The reductions in the effective tax rates for the third quarter and first nine months of fiscal 2012 contributed \$0.02 and \$0.04 to earnings per diluted share, respectively, when compared to the same periods of the prior fiscal year. The change in the effective tax rate (as a percentage of earnings before income taxes) was attributable to the following:

| | Three-Month Period | Nine-Month Period |
|-------------------------------------------------------------------------------------------|-------------------------------|------------------------------|
| Effective tax rate for the period ending June 30, 2011 | 29.1% | 29.7% |
| Repatriation reserve change | | (2.5) |
| Research credit in fiscal 2011 as compared to fiscal 2012 | 1.7 | 2.6 |
| Adjustments of prior period tax issues recorded in the period ending June 30, 2011 | 3.7 | 1.2 |
| Resolution of tax issues with tax authorities recorded in the period ending June 30, 2011 | 0.4 | 0.3 |
| Adjustments of prior period tax issues recorded in the period ending June 30, 2012 | (6.9) | (2.6) |
| Resolution of tax issues with tax authorities recorded in the period ending June 30, 2012 | (2.6) | (0.9) |
| Domestic production activities deduction | (0.1) | (0.4) |
| Foreign tax rate differences | 0.1 | 0.1 |
| Other changes, net | (0.5) | 0.1 |
| Effective tax rate for the period ending June 30, 2012 | 24.9% | 27.6% |

In determining the tax amounts in our financial statements, estimates are sometimes used that are subsequently adjusted in the actual filing of tax returns or by updated calculations. Such adjustments resulted in a net tax benefit of \$2,592 and \$3,429 in the third quarter and first nine months of fiscal 2012, respectively. In fiscal 2011 such adjustments resulted in a net tax benefit of \$1,880 and \$1,607 in the third quarter and first nine months, respectively. In addition, we occasionally have resolutions of tax issues with tax authorities related to prior years due to the conclusion of audits and the lapse of applicable statutes of limitations. Such resolutions resulted in a net tax benefit of \$968 and \$1,130 in the third quarter and first nine months of fiscal 2012, respectively. In fiscal 2011, such resolutions resulted in a net tax benefit of \$191 and \$353 in the third quarter and first nine months, respectively.

During the second quarter of fiscal 2012, we re-evaluated our strategic alternatives in various international markets and determined that a portion of the undistributed earnings of certain of our foreign subsidiaries that were previously expected to be repatriated into the U.S. within the foreseeable future will remain indefinitely invested outside the U.S. to support the growth of our foreign operations. We accordingly reversed the deferred tax liability associated with repatriating those earnings, resulting in a tax benefit of \$3,326 for the nine-months ending June 30, 2012.

On December 17, 2010, legislation was enacted that retroactively extended the U.S. research tax credit, which had expired as of December 31, 2009. As a result of this extension, we recognized a tax benefit of \$3,088 in fiscal 2011 related to the retroactive impact to the prior year. The credit expired again as of December 31, 2011.

Segment Results

In September 2011, we reorganized our reportable segments to better align with our markets. We now have two reportable segments – Aerospace and Energy. Both of our reportable segments are comprised of multiple business groups, which focus on particular applications within the aerospace and energy markets. Our Aerospace segment combines the aircraft propulsion portion of the former Turbine Systems business group, now referred to as the Aircraft Turbine Systems business group, with our Airframe Systems business group. Our Energy segment combines the industrial turbine portion of the former Turbine Systems business group, now referred to as the Industrial Turbomachinery Systems business group, with our Engine Systems and Electrical Power Systems business groups.

Prior period segment information has been retrospectively revised to be consistent with our current reportable segment structure, which is based on how we managed our business as of September 30, 2011 and during the first nine months of fiscal 2012.

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The following table presents sales by segment:

| | Three-Months Ending June 30, | | | | Nine-Months Ending June 30, | | | |
|----------------------------|------------------------------|--------|------------|--------|-----------------------------|--------|--------------|--------|
| | 2012 | | 2011 | | 2012 | | 2011 | |
| External net sales: | | | | | | | | |
| Aerospace | \$ 214,474 | 46.6% | \$ 215,242 | 49.1% | \$ 632,037 | 47.3% | \$ 601,331 | 49.2% |
| Energy | 245,767 | 53.4 | 223,225 | 50.9 | 704,893 | 52.7 | 621,077 | 50.8 |
| Consolidated net sales | \$ 460,241 | 100.0% | \$ 438,467 | 100.0% | \$ 1,336,930 | 100.0% | \$ 1,222,408 | 100.0% |

The following table presents earnings by segment:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-------------------------------------------|------------------------------|-----------|-----------------------------|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Aerospace | \$ 21,536 | \$ 35,402 | \$ 82,277 | \$ 88,557 |
| Energy | 31,205 | 29,251 | 92,264 | 80,695 |
| Total segment earnings | 52,741 | 64,653 | 174,541 | 169,252 |
| Nonsegment expenses | (8,687) | (7,554) | (23,623) | (21,599) |
| Interest expense, net | (6,346) | (6,244) | (18,996) | (18,836) |
| Consolidated earnings before income taxes | 37,708 | 50,855 | 131,922 | 128,817 |
| Income tax expense | (9,406) | (14,799) | (36,452) | (38,272) |
| Consolidated net earnings | \$ 28,302 | \$ 36,056 | \$ 95,470 | \$ 90,545 |

The following table presents earnings by segment as a percentage of segment net sales:

| | Three-Months Ending June 30, | | Nine-Months Ending June 30, | |
|-----------|------------------------------|-------|-----------------------------|-------|
| | 2012 | 2011 | 2012 | 2011 |
| Aerospace | 10.0% | 16.4% | 13.0% | 14.7% |
| Energy | 12.7% | 13.1% | 13.1% | 13.0% |

Aerospace

Aerospace segment net sales were \$214,474 and \$632,037 for the third quarter and first nine months of fiscal 2012, respectively, compared to \$215,242 and \$601,331 for the same periods of fiscal 2011. Aerospace sales in the third quarter of fiscal 2012 were largely consistent when compared to the prior year. Commercial OEM and aftermarket sales in the third quarter of fiscal 2012 improved over the prior year, although lower defense sales largely offset these increases. Increased sales during the first nine months of fiscal 2012 were primarily attributable to strong aftermarket and commercial OEM sales.

Sales for the aerospace aftermarket continued to benefit from increased passenger air traffic, and the roll out of new aircraft platforms on which our Aerospace products are used. Commercial OEM aircraft deliveries of narrow-body and wide-body aircraft have increased based on improved airline demand and new product introduction. In addition, the increase in sales continues to reflect recovering demand for business and regional jets. Due to quarterly variability, defense sales decreased modestly in the third quarter of fiscal 2012 compared to the third quarter of the prior fiscal year. Defense sales for the first nine months of fiscal 2012 were relatively unchanged when compared to the first nine months of the prior year.

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Aerospace segment earnings decreased by \$13,866, or 39.2%, to \$21,536 and \$6,280, or 7.1%, to \$82,277 for the third quarter and first nine months of fiscal 2012, respectively, as compared to \$35,402 and \$88,557, for the same periods of fiscal 2011 due to the following:

| | Three-Month Period | Nine-Month Period |
|---------------------------------------------------------------------------------|-------------------------------|------------------------------|
| Earnings for the period ending June 30, 2011 | \$ 35,402 | \$ 88,557 |
| Sales volume changes | (1,046) | 9,346 |
| Selling price and mix | 4,883 | 14,999 |
| Investments in research and development | (10,570) | (25,490) |
| Manufacturing costs associated with sales growth and manufacturing productivity | (4,103) | (6,459) |
| Workman s compensation | (587) | 2,396 |
| Changes in variable compensation | 643 | 2,325 |
| Other, net | (3,086) | (3,397) |
| Earnings for the period ending June 30, 2012 | \$ 21,536 | \$ 82,277 |

Segment earnings as a percentage of sales decreased to 10.0% and 13.0% for the third quarter and first nine months of fiscal 2012, respectively, compared to 16.4% and 14.7% for the same periods of the prior year. The first nine months of the prior year included a charge of \$2,983 related to workman s compensation. The decrease in Aerospace segment earnings in both the third quarter and first nine months of fiscal 2012 as compared to the same periods of fiscal 2011 was primarily the result of our increased investment in product development and improved production processes resulting from our being awarded a substantial number of significant new system programs, partially offset by favorable price and sales mix and reduced variable compensation expense. Many of the new system programs have expanded more than anticipated in both content and complexity, requiring increased investments in new product development and production process improvements, including programs to streamline production cell layouts and reduce waste in the manufacturing process.

Aerospace segment net sales and earnings for the third quarter of fiscal 2012 were also negatively impacted by the following enterprise resource planning (ERP) system-related issues that have been addressed. We experienced an enterprise wide information technology (IT) system outage related to a hardware failure. Additionally, a faulty system interface with a new supply chain partner led to part shortages. Lastly, we are implementing a new ERP system for our Aerospace motion control business. As a result of these factors we experienced some unanticipated production delays.

Energy

Energy segment net sales were \$245,767 and \$704,893 for the third quarter and first nine months of fiscal 2012, respectively, compared to \$223,225 and \$621,077 for the same periods of fiscal 2011. Net sales for the third quarter and first nine months of fiscal 2012 increased in nearly all of our energy markets. Wind turbine power converter sales increased primarily due to market share gains. In addition, we experienced some accelerated ordering by our customers in an effort to take advantage of current government incentives and to comply with various renewable energy programs. Net sales also increased in our industrial gas turbine markets and our large and small engine markets utilizing natural gas and other special fuel sources, which serve primarily electric power generation systems and on-highway natural gas vehicles.

Energy segment earnings increased by \$1,954, or 6.7%, to \$31,205 and \$11,569, or 14.3%, to \$92,264 for the third quarter and first nine months of fiscal 2012, respectively, as compared to \$29,251 and \$80,695, respectively, for the same periods of fiscal 2011 due to the following:

| | Three-Month Period | Nine-Month Period |
|----------------------------------------------|-------------------------------|------------------------------|
| Earnings for the period ending June 30, 2011 | \$ 29,251 | \$ 80,695 |
| Sales volume changes | 8,236 | 24,758 |
| Selling price and mix | (3,124) | (9,533) |
| Investments in research and development | 250 | (2,698) |
| Changes in variable compensation | 201 | 2,826 |
| Effects of changes in foreign currency rates | (923) | 602 |

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| | | |
|----------------------------------------------|-----------|-----------|
| Other, net | (2,686) | (4,386) |
| Earnings for the period ending June 30, 2012 | \$ 31,205 | \$ 92,264 |

The increase in the Energy segment earnings for both the third quarter and the first nine months of fiscal 2012 as compared to the same periods of fiscal 2011 was driven primarily by increased sales volume and reduced variable compensation, partially offset by unfavorable product mix impacts. Earnings as a percentage of sales decreased slightly to 12.7% in the third quarter of fiscal 2012 compared to 13.1% in the same period of fiscal 2011 due primarily to unfavorable product mix impacts, partially offset by leverage on sales volume. Earnings as a percentage of sales were consistent with the prior year at 13.1% in the first nine months of fiscal 2012 as compared to 13.0% for the same period of fiscal 2011. Segment earnings as a percent of sales were positively impacted by the increase in sales volume, offset by unfavorable product mix and increased investments in research and development.

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Nonsegment expenses for the third quarter and first nine months of fiscal 2012 increased to \$8,687 and \$23,623, respectively, compared to \$7,554 and \$21,599 for the same periods of fiscal 2011. As a percent of net sales, nonsegment expenses for the third quarter and first nine months of fiscal 2012 were 1.9% and 1.8% of net sales, respectively, as compared to 1.7% and 1.8% of net sales, respectively, for the same periods of fiscal 2011.

LIQUIDITY AND CAPITAL RESOURCES

We believe liquidity and cash generation are important to our strategy of self-funding our ongoing operating needs. Historically, we have been able to satisfy our working capital needs, including capital expenditures, product development and other liquidity requirements associated with our operations, with cash flow provided by operating activities. We expect that cash generated from our operating activities, together with borrowings under our revolving credit facility, will be sufficient to fund our continuing operating needs.

As of June 30, 2012, we do not believe that any potential European sovereign debt defaults would have a material adverse affect on our liquidity. We do not have any significant direct exposure to European government receivables, and our customers do not rely heavily on European government subsidies or other government support. We will continue to monitor our exposure to risks relating to European sovereign debt.

Our aggregate cash and cash equivalents were \$39,903 and \$74,539 and our working capital was \$616,047 and \$536,936 at June 30, 2012 and September 30, 2011, respectively. Of the \$39,903 of cash and cash equivalents held at June 30, 2012, \$32,702 is held by our foreign subsidiaries. We are not presently aware of any significant restrictions on the repatriation of these funds, although a portion is considered permanently invested in these foreign subsidiaries. If these funds were needed to fund our operations or satisfy obligations in the U.S., they could be repatriated and their repatriation into the U.S. may cause us to incur additional U.S. income taxes or foreign withholding taxes. Any additional taxes could be offset, in part or in whole, by foreign tax credits. The amount of such taxes and application of tax credits would be dependent on the income tax laws and other circumstances at the time these amounts are repatriated. Based on these variables, it is not practicable to determine the income tax liability that might be incurred if these earnings were to be repatriated.

Our Amended and Restated Revolver Agreement, which we entered into on January 4, 2012, extends the maturity date of our revolving credit facility to January 2017 and provides borrowing capacity of up to \$400,000 with the option to increase total borrowing capacity to up to \$600,000, subject to lenders' participation. In the event we are unable to generate sufficient cash flows from operating activities, we can borrow against our \$400,000 revolving credit facility as long as we are in compliance with all of our debt covenants. Historically, we have used borrowings under our revolving credit facility to meet certain short-term working capital needs as well as strategic uses including repurchases of our stock, payments of dividends and acquisitions. In addition, we have various foreign credit facilities, some of which are tied to net amounts on deposit at certain foreign financial institutions. These foreign credit facilities are generally reviewed annually for renewal. We use borrowings under these foreign credit facilities to finance certain local operations on a periodic basis.

At June 30, 2012, we had no borrowings outstanding from our \$400,000 revolving credit facility and we had \$5,000 of borrowings outstanding from our foreign credit facilities. Short-term borrowing activity during the nine-months ending June 30, 2012 were as follows:

| | |
|---------------------------------------------------------|-----------|
| Maximum daily balance during the period | \$ 61,576 |
| Average daily balance during the period | \$ 40,758 |
| Weighted average interest rate on average daily balance | 1.45% |

At June 30, 2012, we had total outstanding debt of \$413,799 with additional borrowing availability of \$393,667 under our \$400,000 revolving credit facility, net of outstanding letters of credit, and additional borrowing availability of \$14,797 under various foreign credit facilities.

We believe we were in compliance with all our debt covenants at June 30, 2012.

In addition to utilizing our cash resources to fund the working capital needs of our business, we evaluate additional strategic uses of our funds, including the repurchase of our stock, payment of dividends, significant capital expenditures, consideration of strategic acquisitions and other potential uses of cash.

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We believe we have adequate access to several sources of contractually committed borrowings and other available credit facilities. However, we could be adversely affected if the banks supplying our borrowing requirements refuse to honor their contractual commitments, cease lending, or declare bankruptcy. While we believe the lending institutions participating in our credit arrangements are financially capable, recent events in the global credit markets, including the failure, takeover or rescue by various government entities of major financial institutions, have created uncertainty with respect to credit availability.

Our ability to service our long-term debt, to remain in compliance with the various restrictions and covenants contained in our debt agreements and to fund working capital, capital expenditures and product development efforts will depend on our ability to generate cash from operating activities, which in turn is subject to, among other things, future operating performance as well as general economic, financial, competitive, legislative, regulatory, and other conditions, some of which may be beyond our control.

Cash Flows Summary

| | Nine-Months Ending June 30, | |
|--------------------------------------------------------------|----------------------------------------|------------------|
| | 2012 | 2011 |
| Net cash provided by operating activities | \$ 63,653 | \$ 46,800 |
| Net cash used in investing activities | (43,993) | (71,554) |
| Net cash used in financing activities | (51,889) | (9,502) |
| Effect of exchange rate changes on cash and cash equivalents | (2,407) | 1,275 |
| Net change in cash and cash equivalents | (34,636) | (32,981) |
| Cash and cash equivalents at beginning of period | 74,539 | 105,579 |
| Cash and cash equivalents at end of period | \$ 39,903 | \$ 72,598 |

Net cash flows provided by operating activities for the first nine months of fiscal 2012 was \$63,653 compared to \$46,800 for the same period of fiscal 2011. The increase of \$16,853 is primarily attributable to changes in inventory, which utilized \$46,918 of cash in the first nine months of fiscal year 2012 compared to \$77,389 of cash utilized in the first nine months of fiscal 2011.

Net cash flows used in investing activities for the first nine months of fiscal 2012 was \$43,993 compared to \$71,554 for the same period of fiscal 2011. The decrease of \$27,561 compared to the same period of the prior fiscal year is due primarily to the acquisition of Integral Drive Systems AG and its European companies (IDS), and the assets of IDS 's business in China (collectively, the IDS Acquisition) completed in the third quarter of fiscal 2011 utilizing net cash of \$47,161. Cash paid for capital expenditures was \$44,224 during the first nine months of fiscal 2012, compared to \$32,640 during the same period of fiscal 2011.

Net cash flows used in financing activities for the first nine months of fiscal 2012 was \$51,889 as compared to \$9,502 for the same period of fiscal 2011. We utilized \$31,881 to repurchase 792 shares of our common stock in the first nine months of fiscal 2012, compared to \$6,837 to repurchase 208 shares of our common stock in the same period of fiscal 2011. In addition, during the first nine months of fiscal 2012, we had net debt repayments of \$11,500 compared to net borrowings of \$6,440 in the same period of the prior year.

Contractual Obligations

We have various contractual obligations, including obligations related to long-term debt, operating leases, purchases, retirement pension benefit plans, and other postretirement benefit plans. These contractual obligations are summarized and discussed more fully in Management 's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of our most recent Form 10-K. There have been no material changes to our various contractual obligations during the first nine months of fiscal 2012 other than those relating to certain of our credit facilities and our Term Loan Credit Agreement, dated as of October 1, 2008, as amended, as discussed at Note 12, *Credit facilities, short-term borrowings and long-term debt*, in the Notes to the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Form 10-Q.

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Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires us to make judgments, assumptions, and estimates that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Note 1, *Operations and summary of significant accounting policies*, to the Consolidated Financial Statements in our most recent Form 10-K describes the significant accounting policies and methods used in the preparation of the Consolidated Financial Statements. The estimates and assumptions described below are those that we consider to be most critical to an understanding of our financial statements because they involve significant judgments and uncertainties. All of these estimates reflect our best judgment about current and, for some estimates, future economic and market conditions and their effects based on information available as of the date of these financial statements. As estimates are updated or actual amounts are known, our critical accounting estimates are revised, and operating results may be affected by the revised estimates. Actual results may differ from these estimates under different assumptions or conditions.

Our management has discussed the development and selection of these critical accounting estimates with the Audit Committee of our Board of Directors, and the Audit Committee has reviewed our disclosures in this Management's Discussion and Analysis.

Revenue recognition

Except for revenues recognized under the percentage of completion method discussed below, Woodward recognizes revenue when the following criteria are met:

- 1) persuasive evidence of an arrangement exists,
- 2) delivery of the product has occurred or services have been rendered,
- 3) price is fixed or determinable, and
- 4) collectability is reasonably assured.

In implementing the four criteria stated above, we have found that determining when the risks and rewards of ownership have passed to the customer, which determines whether persuasive evidence of an arrangement exists and if delivery has occurred, may require judgment. The passage of title indicates transfer of the risks and rewards of ownership from Woodward to the customer; however, contract- and customer-specific circumstances are reviewed by management to ensure that transfer of title constitutes the transfer of the risks and rewards of ownership.

Examples of situations requiring management review and judgment, with respect to the passage of the risks and rewards of ownership, include: interpretation of customer-specific contract terms, situations where substantive performance obligations exist, such as completion of product testing that remain after product delivery to the customer, situations that require customer acceptance (or in some instances regulatory acceptance) of the product, and situations in countries whose laws provide for retention of some form of title by sellers such that Woodward is able to recover goods in the event a customer defaults on payment.

Based on management's determination, if the risks and rewards of ownership have not passed to the customer, revenue is deferred until this requirement is met.

Woodward provides certain engineering services to customers under fully funded and partially funded long- and short-term development contracts, which accounted for an immaterial amount of customer payments received in the three and nine-months ending June 30, 2012 and June 30, 2011. Funded development contracts may be fixed price or cost-reimbursable contracts. Revenue for such contracts is recognized using the percentage-of-completion, milestone or completed contract methods. The applicable revenue recognition methodology to apply is dependent on an evaluation of each project.

Estimating total anticipated costs on long-term projects requires a comprehensive understanding and consideration of variables that may impact the future costs required to be incurred to complete the project, and are subject to revision and adjustment throughout the projects. Accurately estimating total costs on long-term contracts is often difficult due to the number of variables to consider, including customer changes to project scope, unexpected engineering charges and cost overruns. Changes in estimates over the course of a project will impact the future timing of revenue recognition on projects accounted for using the percentage-of-completion method and the milestone method, as well as the timing of recognition of loss reserves, if any.

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Changes in contract estimates occur for a variety of reasons, including changes in contract scope, changes in contract cost estimates due to unanticipated cost growth, changes in risks affecting contract costs and/or the resolution of contract risks at lower costs than anticipated, and changes in contract overhead costs over the performance period. The Company has a contract management process involving cross-functional groups who are familiar with our contract activities. Significant changes in estimates on a single contract could impact our financial results. Aggregate net changes in contract estimates recognized on a cumulative catch-up basis were not material to our Condensed Consolidated Financial Statements for the three and nine-months ending June 30, 2012 and June 30, 2011. No discrete event or adjustment to an individual contract within the aggregate net changes in contract estimates for three and nine-months ending June 30, 2012 and June 30, 2011 was material to the Condensed Consolidated Financial Statements for such period.

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Purchase accounting

During the third quarter of fiscal 2011, we completed the IDS Acquisition for an aggregate purchase price of \$47,161. For more information on the IDS Acquisition see Note 4, *Business acquisitions*, in the Notes to the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Form 10-Q.

Assigning fair market values to the assets acquired and liabilities assumed at the date of an acquisition requires knowledge of current market values, and the values of assets in use, and often requires the application of judgment regarding estimates and assumptions. While the ultimate responsibility resides with management, for material acquisitions, we retain the services of certified valuation specialists to assist with assigning estimated values to certain acquired assets and assumed liabilities, including intangible assets and postretirement benefit plan assets and liabilities.

Acquired intangible assets, excluding goodwill, are valued using a discounted cash flow methodology based on future cash flows. This methodology incorporates various estimates and assumptions, the most significant being projected revenue growth rates, earnings margins, and forecasted cash flows based on the discount rate and terminal growth rate. Management projects revenue growth rates, earnings margins and cash flows based on the historical operating results of the acquired entity adjusted for synergies anticipated to be achieved through integration, expected future performance, operational strategies, and the general macroeconomic environment. We review finite-lived intangible assets for triggering events such as significant changes in operations, customers or future revenue that might indicate the need to impair the assets acquired or change the useful lives of the assets acquired. In the three and nine-months ending June 30, 2012 and June 30, 2011, no impairment or change in useful lives has been recognized on other intangible assets acquired.

Estimated values for inventory acquired is subject to reliable estimates of future sales volumes, replacement costs, costs of selling effort, anticipated selling prices, normal profit margins and the percent complete, as of the acquisition date, and costs to complete work-in-process inventory. Estimated values for accounts receivable are subject to reliable estimates of collectability.

Assumed liabilities are valued based on estimates of anticipated expenditures to be incurred to satisfy the assumed obligations, including estimation of any warranty or other contractual liabilities assumed, which require the exercise of professional judgment. Valuation of postretirement benefit plan assets and liabilities is dependent on similar assumptions and estimates as those used to value our non-acquisition postretirement benefit plan assets and liabilities.

Assumed contracts may have favorable or unfavorable terms that must be valued as of the acquisition date. Such valuation is subject to management judgment regarding the evaluation and interpretation of contract terms in relation to other economic circumstances, such as the market rates for office space leases.

If we assume a performance obligation to customers as of the acquisition date, a deferred revenue obligation is recognized. Judgment is required to evaluate whether a future performance obligation exists and to assign a value to the performance obligation.

Valuation of gain and loss contingencies, if not resolved during the purchase measurement period, requires exercise of management judgment. We measure pre-acquisition contingencies at their acquisition date fair value if their fair value can be determined during the measurement period. If we cannot determine the fair value of the pre-acquisition contingency during the measurement period, we recognize an acquired asset or assumed liability if it is probable that an asset existed or that a liability had been incurred at the acquisition date and the amount of the asset or liability can be reasonably estimated.

Assumed acquired tax liabilities for uncertain tax positions are dependent on assessing the past practices of the acquisition target based on review of actual tax filings and information obtained through due diligence procedures. Evaluation of the validity of tax positions taken by the acquisition target are subject to management judgment.

Inventory

Inventories are valued at the lower of cost or market value. Inventory cost is determined using methods that approximate the first-in, first-out basis. We include product costs, labor and related fixed and variable overhead in the cost of inventories.

Inventory market values are determined by giving substantial consideration to the expected product selling price. We estimate expected selling prices based on our historical recovery rates, general economic and market conditions, the expected channel of disposition, and current customer contracts and preferences. Actual results may differ from our estimates due to changes in resale or market value and the mix of these factors. Management monitors inventory for events or circumstances, such as negative margins, recent sales history suggesting lower sales value, or

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changes in customer preferences, which indicate the market value of inventory is less than the carrying value of inventory and records adjustments as necessary. When inventory is written down below cost, such reduced amount is considered the cost for subsequent accounting purposes. Our recording of inventory at the lower of cost or market value has not historically required material adjustments once initially established.

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The carrying value of inventory was \$423,994 and \$381,555 as of June 30, 2012 and September 30, 2011, respectively. If economic conditions, customer product requirements or other factors significantly reduce future customer demand for our products from forecast levels, then future adjustments to the carrying value of inventory may become necessary. We attempt to maintain inventory quantities at levels considered necessary to fill expected orders in a reasonable time frame, which we believe mitigates our exposure to future inventory carrying cost adjustments.

Postretirement benefits

The Company provides various benefits to certain employees through defined benefit plans and other postretirement benefit plans. A September 30 measurement date is utilized to value plan assets and obligations for all Woodward defined benefit pension and other postretirement benefit plans. For financial reporting purposes, net periodic benefits expense and related obligations are calculated using a number of significant actuarial assumptions, including anticipated discount rates, rates of compensation increases, long-term return on defined benefit plan investments, and anticipated healthcare cost increases. Based on these actuarial assumptions, at September 30, 2011, our recorded liabilities included \$25,349 for underfunded defined benefit pension plans and \$32,923 for unfunded other postretirement benefit plans. Changes in net periodic expense or the amounts of recorded liabilities may occur in the future due to changes in these assumptions.

Estimates of the value of postretirement benefit obligations, and related net periodic benefits expense, are dependent on actuarial assumptions, including future interest rates, compensation rates, healthcare cost trends, and returns on defined benefit plan investments.

Primary actuarial assumptions for our defined benefit plans were determined as follows:

The discount rate assumption is intended to reflect the rate at which the retirement benefits could be effectively settled based upon the assumed timing of the benefit payments. In the U.S., we used a bond portfolio matching analysis based on recently traded, non-callable bonds rated AA or better, which have at least \$50 million outstanding. In the United Kingdom, we used the iBoxx AA-rated corporate bond index (applicable for bonds over 15 years) to determine a blended rate to use as the benchmark. In Japan, we used Standard & Poors AA-rated corporate bond yields (applicable for bonds over 10 years) as the benchmark. In Switzerland, we used high quality swap rates plus a credit spread of 0.36%, as high quality swaps are available in Switzerland at various durations and trade at higher volumes than bonds, as the benchmark. Our assumed rates do not differ significantly from any of these benchmarks. These rates are sensitive to changes in interest rates. A decrease in the discount rate would increase our obligation and future expense.

Compensation increase assumptions are based upon historical experience and anticipated future management actions. An increase in the rate would increase our obligation and expense.

In determining the long-term rate of return on plan assets, we assume that the historical long-term compound growth rates of equity and fixed-income securities will predict the future returns of similar investments in the plan portfolio. Investment management and other fees paid out of the plan assets are factored into the determination of asset return assumptions. This rate is impacted by changes in general market conditions, but because it represents a long-term rate, it is not significantly impacted by short-term market volatility. Changes in our allocation of plan assets would also impact this rate. For example, a shift to more fixed income securities would lower the rate. A decrease in the rate would increase our expense.

Primary actuarial assumptions for our other postretirement benefit plans were determined as follows:

The discount rate assumption is intended to reflect the rate at which the postretirement benefits could be effectively settled based upon the assumed timing of the benefit payments. In the U.S., we used a bond portfolio matching analysis based on recently traded, non-callable bonds rated AA or better, which have at least \$50 million outstanding. In the United Kingdom, we used the iBoxx AA-rated corporate bond index (applicable for bonds over 15 years) to determine a blended rate to use as the benchmark. Our assumed rate did not differ significantly from this benchmark. These rates are sensitive to changes in interest rates. A decrease in the discount rate would increase our obligation and future expense.

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The assumed health care trend rate represents the rate at which health care costs are assumed to increase and is based on historical and expected experience. Changes in our projections of future health care costs due to general economic conditions and those specific to health care (e.g., technology driven cost changes) will impact this trend rate. An increase in the trend rate would increase our obligation and expense.

Variances from our fiscal year end estimates for these variables could materially affect our recognized postretirement benefit obligation liabilities. On a near-term basis, such changes are unlikely to have a material impact on reported earnings, since such adjustments are recorded to other comprehensive earnings and recognized into expense over a number of years. Significant changes in estimates could, however, materially affect the carrying amounts of benefit obligation liabilities, including accumulated benefit obligations, which could affect compliance with the provisions of our debt arrangements and future borrowing capacity.

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The following information illustrates the sensitivity of the net periodic benefit cost and the projected accumulated benefit obligation to a change in the discount rate assumed.

| Assumption | Change | Increase/(Decrease) In | | |
|------------------------------------------|-------------|--------------------------------|-------------------------------------------|---------------------------------------------------------|
| | | 2012 Net Periodic Benefit Cost | 2012 Projected Service and Interest Costs | Post Retirement Benefit Obligation as of Sept. 30, 2011 |
| Defined benefit pension benefits: | | | | |
| Change in discount rate | 1% increase | \$ (1,327) | \$ (443) | \$ (21,575) |
| | 1% decrease | 2,358 | 403 | 26,480 |
| Other postretirement benefits: | | | | |
| Change in discount rate | 1% increase | (116) | 140 | (2,584) |
| | 1% decrease | (10) | (172) | 2,998 |

It should be noted that economic factors and conditions often affect multiple assumptions simultaneously, and the effects of changes in assumptions are not necessarily linear due to factors such as the 10% corridor applied to the larger of the postretirement benefit obligation or the fair market value of plan assets when determining amortization of actuarial net gains or losses.

A one-percentage-point change in assumed health care cost trend rates would have the following effects:

| | 1% increase | 1% decrease |
|-------------------------------------------------------------------------------|-------------|-------------|
| Effect on projected fiscal year 2012 service and interest cost | \$ 182 | \$ (159) |
| Effect on accumulated postretirement benefit obligation at September 30, 2011 | 3,107 | (2,722) |

Reviews for impairment of goodwill

At June 30, 2012, we had \$460,509 of goodwill, representing 26% of our total assets. At September 30, 2011, we had \$462,282 of goodwill, representing 26% of our total assets. Goodwill is tested for impairment on the individual or aggregate reporting unit level, as appropriate, on an annual basis and more often if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. For purposes of performing the impairment tests, we identify reporting units in accordance with U.S. GAAP. The identification of reporting units and consideration of aggregation criteria requires management judgment. The impairment tests consist of comparing the fair value of reporting units, determined using discounted cash flows, with its carrying amount including goodwill. If the carrying amount of the reporting unit exceeds its fair value, we compare the implied fair value of goodwill with its carrying amount. If the carrying amount of goodwill exceeds the implied fair value of goodwill, an impairment loss would be recognized to reduce the carrying amount to its implied fair value. There was no impairment charge recorded in the three or nine-months ending June 30, 2012 or in fiscal years 2011 or 2010.

Woodward completed its annual goodwill impairment test as of July 31, 2011 during the quarter ended September 30, 2011. As a part of that test, the fair value of each of Woodward's reporting units was determined using a discounted cash flow method. This method represents a Level 3 input and incorporates various estimates and assumptions, the most significant being projected revenue growth rates, operating earnings margins, and forecasted cash flows based on the discount rate and terminal growth rate. Management projects revenue growth rates, operating earnings margins and cash flows based on each reporting unit's current operational results, expected performance and operational strategies over a five or ten-year period. These projections are adjusted to reflect current economic conditions and demand for certain products, and require considerable management judgment.

Forecasted cash flows used in the July 31, 2011 impairment test were discounted using weighted-average cost of capital assumptions from 10.0% to 10.2%. The terminal values of the forecasted cash flows were calculated using the Gordon Growth Model and assumed an annual compound growth rate after five or ten years of 4.3%. These inputs, which are unobservable in the market, represent management's best estimate of what market participants would use in determining the present value of the Company's forecasted cash flows. Changes in these estimates and assumptions can have a significant impact on the fair value of forecasted cash flows. Woodward evaluated the reasonableness of the reporting units resulting fair values utilizing a market multiple method.

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The results of Woodward's annual goodwill impairment test performed as of July 31, 2011, indicated the estimated fair value of each reporting unit was substantially in excess of its carrying value, and accordingly, no impairment existed. Increasing the discount rate by 20%, decreasing the growth rate by 20%, or decreasing forecasted cash flow by 20%, would not have resulted in an impairment charge at July 31, 2011.

As part of the Company's ongoing monitoring efforts, Woodward will continue to consider the global economic environment and its potential impact on Woodward's business in assessing goodwill recoverability. There can be no assurance that Woodward's estimates and assumptions regarding forecasted cash flows of certain reporting units, the period or strength of the current economic recovery, or the other inputs used in forecasting the present value of forecasted cash flows will prove to be accurate projections of future performance.

Income taxes

We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgment is required in evaluating our tax positions and determining our provision for income taxes.

During the ordinary course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. We establish reserves for tax-related uncertainties based on estimates of whether, and the extent to which, additional taxes will be due. The reserves are established when we believe that certain positions are likely to be challenged and may not be fully sustained on review by tax authorities. We adjust these reserves in light of changing facts and circumstances, such as the closing of a tax audit or refinement of an estimate. Although we believe our reserves are reasonable, no assurance can be given that the final outcome of these matters will be consistent with what is reflected in our historical income tax provisions and accruals. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact the provision for income taxes. The provision for income taxes includes the impact of reserve provisions and changes to reserves that are considered appropriate. As of June 30, 2012 and September 30, 2011, unrecognized gross tax benefits for which recognition has been deferred was \$17,837 and \$16,931, respectively.

Significant judgment is also required in determining any valuation allowance recorded against deferred tax assets. In assessing the need for a valuation allowance, we consider all available evidence including past operating results, estimates of future taxable income, and the feasibility of tax planning strategies. In the event we change our determination as to the amount of deferred tax assets that can be realized, we will adjust our valuation allowance with a corresponding impact to the provision for income taxes in the period in which such determination is made. As of June 30, 2012 and September 30, 2011, our valuation allowance was \$2,699 and \$3,201, respectively.

Our effective tax rates differ from the U.S. statutory rate primarily due to the tax impact of foreign operations, adjustments of valuation allowances, research tax credits, state taxes, and tax audit settlements.

Our provision for income taxes is subject to volatility and could be affected by earnings that are different than those anticipated in countries which have lower or higher tax rates; by changes in the valuation of our deferred tax assets and liabilities; by transfer pricing adjustments; by tax effects of share-based compensation; and/or changes in tax laws, regulations, and accounting principles, including accounting for uncertain tax positions, or interpretations thereof. In addition, we are subject to examination of our income tax returns by the U.S. Internal Revenue Service and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these examinations will not have a significant effect on our operating results, financial condition, and cash flows.

New Accounting Standards

From time to time, the Financial Accounting Standards Board (FASB) or other standards-setting bodies issue new accounting pronouncements. Updates to the FASB Accounting Standards Codification are communicated through issuance of an Accounting Standards Update. Unless otherwise discussed, we believe that the impact of recently issued guidance, whether adopted or to be adopted in the future, is not expected to have a material impact on our Condensed Consolidated Financial Statements upon adoption.

To understand the impact of recently issued guidance, whether adopted or to be adopted, please review the information provided in Note 2, *Recent accounting pronouncements*, in the Notes to the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Form 10-Q.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

In the normal course of business, we have exposures to interest rate risk from our long-term and short-term debt, and our postretirement benefit plans, and foreign currency exchange rate risk related to our foreign operations and foreign currency transactions. We are also exposed to various market risks that arise from transactions entered into in the normal course of business related to items such as the cost of raw materials and changes in inflation. Certain contractual relationships with customers and vendors mitigate risks from changes in raw material costs and foreign currency exchange rate changes that arise from normal purchasing and normal sales activities.

These market risks are discussed more fully in Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of our most recent Form 10-K. These market risks have not materially changed since the date our most recent Form 10-K was filed with the SEC.

Item 4. Controls and Procedures

We have established disclosure controls and procedures, which are designed to ensure that information required to be disclosed in reports filed or submitted under the Securities Exchange Act of 1934 (the Act) is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms. These disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Act is accumulated and communicated to management, including our Principal Executive Officer (Thomas A. Gendron, Chairman of the Board, Chief Executive Officer and President) and Principal Financial and Accounting Officer (Robert F. Weber, Jr., Vice Chairman, Chief Financial Officer and Treasurer), as appropriate, to allow timely decisions regarding required disclosures.

Thomas A. Gendron and Robert F. Weber, Jr., evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Form 10-Q. Based on their evaluations, they concluded that our disclosure controls and procedures were effective as of June 30, 2012.

Furthermore, there have been no changes in our internal control over financial reporting during the fiscal quarter covered by this Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Beginning with the third quarter of fiscal 2012, management included the internal controls of IDS in its assessment of the effectiveness of Woodward's internal controls over financial reporting. IDS was acquired during the third quarter of fiscal 2011, as discussed in Note 4, *Business acquisitions*, in the Notes to the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Form 10-Q, and was excluded from management's annual report on internal control over financial reporting for the fiscal year ended September 30, 2011 in accordance with the general guidance issued by the SEC regarding exclusion of certain acquired businesses. IDS will be included in the September 30, 2012 assessment of Woodward's internal controls over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Woodward is currently involved in claims, pending or threatened litigation or other legal proceedings, investigations or regulatory proceedings arising in the normal course of business, including, among others, those relating to product liability claims, employment matters, workman's compensation claims, regulatory, legal or contractual disputes, product warranty claims and alleged violations of various environmental laws. We have accrued for individual matters that we believe are likely to result in a loss when ultimately resolved using estimates of the most likely amount of loss.

While the outcome of pending claims, proceedings and investigations cannot be predicted with certainty, management believes that any liabilities that may result from these claims, proceedings and investigations will not have a material effect on Woodward's liquidity, financial condition, or results of operations.

Item 1A. Risk Factors

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Investment in our securities involves risk. An investor or potential investor should consider the risks summarized under the caption Risk Factors in Part I, Item 1A of our most recent Form 10-K when making investment decisions regarding our securities. The risk factors that were disclosed in our most recent Form 10-K have not materially changed since the date our most recent Form 10-K was filed with the SEC.

Table of Contents**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**
Issuer Purchases of Equity Securities

| <i>(In thousands, except for shares and per share amounts.)</i> | Total Number of Shares Purchased | Weighted Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1) | Maximum Number (or Approximate Dollar Value) of Shares that may yet be Purchased under the Plans or Programs at Period End (1) |
|-----------------------------------------------------------------|----------------------------------------|---------------------------------------------|--------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------|
| April 1, 2012 through April 30, 2012 (1) | 46,528 | \$ 42.35 | 46,528 | \$ 173,880 |
| May 1, 2012 through May 31, 2012 (1) | 400,000 | 39.00 | 400,000 | 158,281 |
| June 1, 2012 through June 30, 2012 (2) | 556 | 39.44 | | 158,281 |

- (1) In July 2010, our Board of Directors authorized a stock repurchase program of up to \$200,000 of our outstanding shares of common stock on the open market or in privately negotiated transactions over a three-year period that will end in July 2013.
- (2) The Woodward Executive Benefit Plan, which is a separate legal entity, acquired 556 shares of common stock on the open market related to the reinvestment of dividends for shares of treasury stock held for deferred compensation in June 2012. Shares owned by the Woodward Executive Benefit Plan are included in "Treasury stock held for deferred compensation" in the Condensed Consolidated Balance Sheets.

Item 6. Exhibits

- (a) Exhibits filed as Part of this Report are listed in the Exhibit Index.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WOODWARD, INC.

Date: July 23, 2012

/s/ THOMAS A. GENDRON
Thomas A. Gendron
Chairman of the Board, Chief Executive Officer,

and President

(Principal Executive Officer)

Date: July 23, 2012

/s/ ROBERT F. WEBER, JR.
Robert F. Weber, Jr.
Vice Chairman, Chief Financial Officer and

Treasurer

(Principal Financial and Accounting Officer)

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WOODWARD, INC.

EXHIBIT INDEX

| Exhibit Number | Description: |
|----------------|--------------------------------------------------------------------------------------|
| 31.1 | Rule 13a-14(a)/15d-14(a) certification of Thomas A. Gendron, filed as an exhibit. |
| 31.2 | Rule 13a-14(a)/15d-14(a) certification of Robert F. Weber, Jr., filed as an exhibit. |
| 32.1 | Section 1350 certifications, filed as an exhibit. |
| 101.INS | XBRL Instance Document. * |
| 101.SCH | XBRL Taxonomy Extension Schema Document. * |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. * |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document. * |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document. * |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document. * |

* Submitted electronically herewith.

Attached as Exhibit 101 to this report are the following materials from Woodward, Inc.'s Quarterly Report on Form 10-Q for the quarter ending June 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Statements of Earnings, (ii) the Condensed Consolidated Statements of Comprehensive Earnings, (iii) the Condensed Consolidated Balance Sheets, (iv) the Condensed Consolidated Statements of Cash Flows, (v) the Condensed Consolidated Statements of Stockholders' Equity, and (vi) the Notes to the Condensed Consolidated Financial Statements.